

REPORT OF EXAMINATION

**HARLAN INDEPENDENT
SCHOOL DISTRICT**

**FOR THE SCHOOL YEAR
ENDED JUNE 30, 2008**

Gaw & Associates, PLLC

Certified Public Accountants

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CERTIFIED PUBLIC ACCOUNTANTS

Independent Auditor's Report

To the Board of Education
Harlan Independent School District

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Harlan Independent School District, as of and for the year ended June 30, 2008, which collectively comprise the District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of Harlan Independent School District's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the provisions of Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and the audit requirements prescribed by the Kentucky State Committee for School District Audits in *Guide for Auditing Local School Districts' Fiscal Records*. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Harlan Independent School District, as of June 30, 2008, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated October 31, 2008, on our consideration of the Harlan Independent School District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in conjunction with this report in considering the results of our audit.

The management's discussion and analysis and budgetary comparison information on pages 3 through 11 and 35 through 40 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Harlan Independent School District's basic financial statements. The additional information shown on pages 41 through 54 is presented for purposes of additional analysis and is not a required part of the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements of Harlan Independent School District. The additional information shown on pages 41 through 54 and the schedule of expenditures of federal awards has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.



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October 31, 2008



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Management Discussion & Analysis (MD&A)

The discussion and analysis of Harlan Independent School District's financial performance provides an overview of the district's financial activities for the fiscal year ended June 30, 2008 ("FY 2008"). The intent of this discussion and analysis is to look at the district's financial performance as a whole. Readers should also review the basic financial statements along with the notes to these statements to enhance their understanding of the district's financial performance.

Financial Highlights

Key financial highlights for FY 2008 are as follows:

- The ending cash balance for the District was \$1.8 million in 2008 and \$2.4 million in 2007. This change was the result of construction expenditures, excess expenses over revenues in food service and non reimbursement of special revenue fund by fiscal year end.
- From 2007 to 2008 total general fund revenue increased by 11%.
- Among major funds, the General Fund had \$5.5 million in revenue, which primarily consists of ad valorem, utility, federal and state funding (the SEEK program). There were \$5.3 million in expenditures.

Using the Annual Report

This annual financial report contains, in addition to this Management Discussion and Analysis, the district's basic financial statements and supplementary information. These three sections together provide a comprehensive overview of the district's finances. The basic financial statements are comprised of two kinds of statements that present financial information from different perspectives, district-wide and funds.

- District-wide financial statements, which comprise the first two statements, provide both short-term and long term information about the district's overall financial position.
- Individual parts of the district, which are reported as fund financial statements, focus on reporting the district's operation in more detail. These fund financial statements comprise the remaining statements.

Notes to the financials, which are included just following the basic financial statements, provide more detailed data and explain some of the information in the statements. The supplementary information sections provide further explanations and additional support for the financial statements, including a comparison of the district's budget to actual revenues and expenditures for the year.

Additional elements of this report include sections on State and Federal Award Compliance and Findings and Recommendations.

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Overview of the Financial Statements

District-wide Financial Statements – Statement of Net Assets and the Statement of Activities

While this document contains specific information on the many funds used by the district to provide programs and activities, the view of the district as a whole looks at all financial transactions and asks the question, “How did we do financially during the previous year?” The *Statement of Net Assets* and the *Statement of Activities* answer this question. These statements include all assets and liabilities using the accrual basis of accounting similar to the accounting used by most private-sector companies. This basis of accounting takes into account all of the current year revenues and expenses regardless of when cash is received or paid.

These two statements report the district’s net assets and changes in those assets. This change in net assets is important because it tells the reader that, for the district as a whole, the financial position of the district has either improved or diminished. The causes of this change may be the result of many factors, some financial, and some not. Non-financial factors include the district’s property tax base, current property tax laws in Kentucky, facility condition, required educational programs and other factors.

In the *Statement of Net Assets* and the *Statement of Activities*, the district reports governmental activities. Governmental activities are the activities where most of the district’s programs and services are reported including, but not limited to, instruction, support services, operation and maintenance of plants and facilities, pupil transportation and extracurricular activities. The district does not have any business-type activities.

The district-wide financial statements can be found on pages 12 – 13 of this report.

Fund Financial Statements

The analysis of the district’s major funds begins on page 14. Fund financial reports provided detailed information about the district’s major funds. The district uses several funds to account for a multitude of financial transactions. However, these fund financial statements focus on the district’s most significant funds and not the district as a whole. The district’s major governmental funds are the General Fund, Special Revenue Fund, and the Construction Fund.

Governmental Funds

Nearly all of this district activities are reported in governmental funds. Governmental fund financial statements focus on how money flows into and out of these funds and the balance left at year-end available for spending in future periods. These funds are reported using an accounting method called modified accrual accounting, which measures cash and all other financial assets that can readily be converted to cash. The governmental fund statements provide a detailed short-term view of the district’s general government operations and the basic services it provides. Governmental fund information helps you to determine whether there are more or fewer financial resources that can be spent in the near future to finance educational programs. The relationship (or differences) between governmental activities (reported in the *Statement of Net Assets* and the *Statement of Activities*) and governmental funds is reconciled in the financial statements.

Fiduciary Funds

The district is the trustee, or fiduciary, for student body funds. All of the district’s fiduciary activities are reported in a separate *Statement of Fiduciary Net Assets and Liabilities* on page 20. We exclude

these activities from the district's other financial statements because the district cannot use these assets to finance its operations.

Notes to the Basic Financial Statement

The notes provide additional information that is essential to a full understanding of the data provided in the district-wide and fund financial statements. The notes to the financial statements can be found starting on page 22 of this report.

Financial analysis of the District as a Whole

As stated earlier the *Statement of Net Assets* and the *Statement of Activities* provide a financial glimpse of the District as a whole. Table 1 (Net Assets Summary) provides a summary of the district's net assets for FY 2008 as contained in the Statement of Net Assets and compares that information to FY 2007. As the table shows, our total net assets as of June 30, 2008 were \$5.0 million, an increase of \$469 thousand from the prior year.

Table 1: Summary of Net Assets

	June 30, 2007	June 30, 2008	Change	Percentage Change
Assets				
Current and Other Assets	\$ 2,804,724	\$ 2,038,052	\$ (766,672)	-27%
Capital Assets	6,865,430	7,802,129	936,699	14%
<i>Total Assets</i>	<u>9,670,154</u>	<u>9,840,181</u>	<u>170,027</u>	<u>2%</u>
Liabilities				
Current Liabilities	510,012	625,045	115,033	23%
Long-Term Liabilities	4,552,270	4,138,218	(414,052)	-9%
<i>Total Liabilities</i>	<u>5,062,282</u>	<u>4,763,263</u>	<u>(299,019)</u>	<u>-6%</u>
Net Assets				
Invested in Capital Assets, Net of Debt	2,313,160	2,243,098	(70,062)	-3%
Restricted	1,626,941	1,534,055	(92,886)	-6%
Unrestricted	667,771	1,299,765	631,994	95%
<i>Total Net Assets</i>	<u>\$ 4,607,872</u>	<u>\$ 5,076,918</u>	<u>\$ 469,046</u>	<u>10%</u>

In comparing FY 2008 to the prior year we note the following:

- Current assets decreased because of expenditures for construction costs.
- Capital assets increased because of construction.
- Long-term liabilities decreased because of a bond payments.

Table 2 (Change in Net Assets) reflects data extracted from the *Statement of Activities* and shows the changes in net assets from FY 2007 to FY 2008.

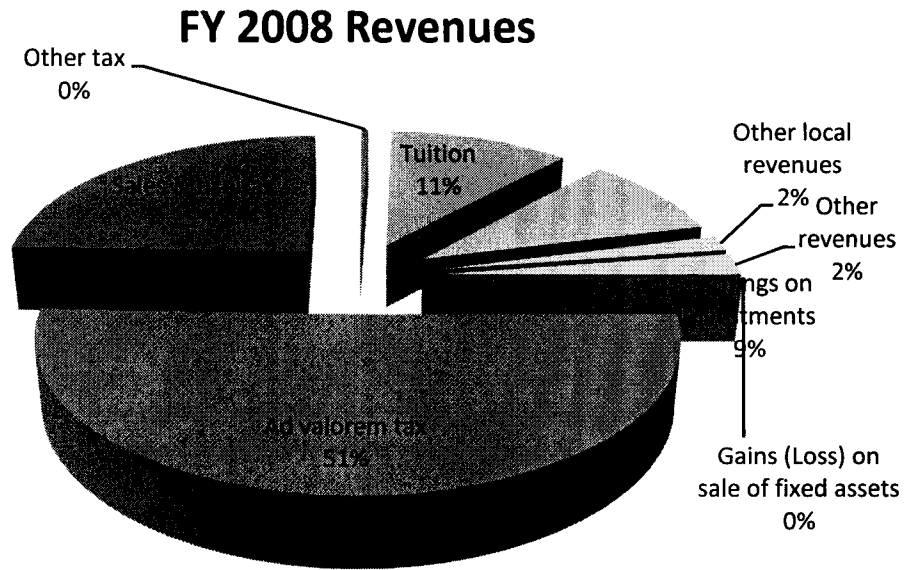
Table 2: Changes in Net Assets

	June 30, 2007	June 30, 2008	Change	Percentage Change
Revenues				
Program Revenues:				
Charges for Services	203,498	203,311	(187)	0%
Operating Grants and Contributions	5,906,982	6,588,776	681,794	12%
Capital Grants and Contributions	207,688	337,725	130,037	63%
General Revenues:				
Ad valorem tax	478,365	471,275	(7,090)	-1%
Sales & use tax	220,517	228,136	7,619	3%
Other tax	3,276	4,348	1,072	33%
Tuition	47,784	104,665	56,881	119%
Earnings on investments	93,254	84,953	(8,301)	-9%
Other local revenues	4,896	15,275	10,379	212%
Total local revenue	848,092	908,652	60,560	7%
Other revenues	28,678	22,282	(6,396)	-22%
Gains (Loss) on sale of fixed assets		105	105	100%
Total Revenues	7,194,938	8,060,851	865,913	12%
Program Expenses:				
Instruction	\$ 3,809,648	\$ 4,248,442	438,794	12%
Support services				
Student	267,798	273,495	5,697	2%
Instruction staff	913,719	395,102	(518,617)	-57%
District administration	357,556	441,586	84,030	24%
School administration	341,318	388,961	47,643	14%
Business	104,365	103,154	(1,211)	-1%
Plant operation and maintenance	629,152	739,716	110,564	18%
Student transportation	318,295	181,386	(136,909)	-43%
Total support services	2,932,203	2,523,400	(408,803)	-14%
Community service activities	111,282	111,186	(96)	0%
Bond Issuance Cost	4,324		(4,324)	100%
Interest Expense	171,946	156,248	(15,698)	-9%
Food Service	-	431,164	431,164	100%
Non-major Fund	-	94,597	94,597	100%
Total Expenses	7,029,403	7,565,037	535,634	8%
Change in Net Assets	\$ 165,535	\$ 495,814	\$ 330,279	200%

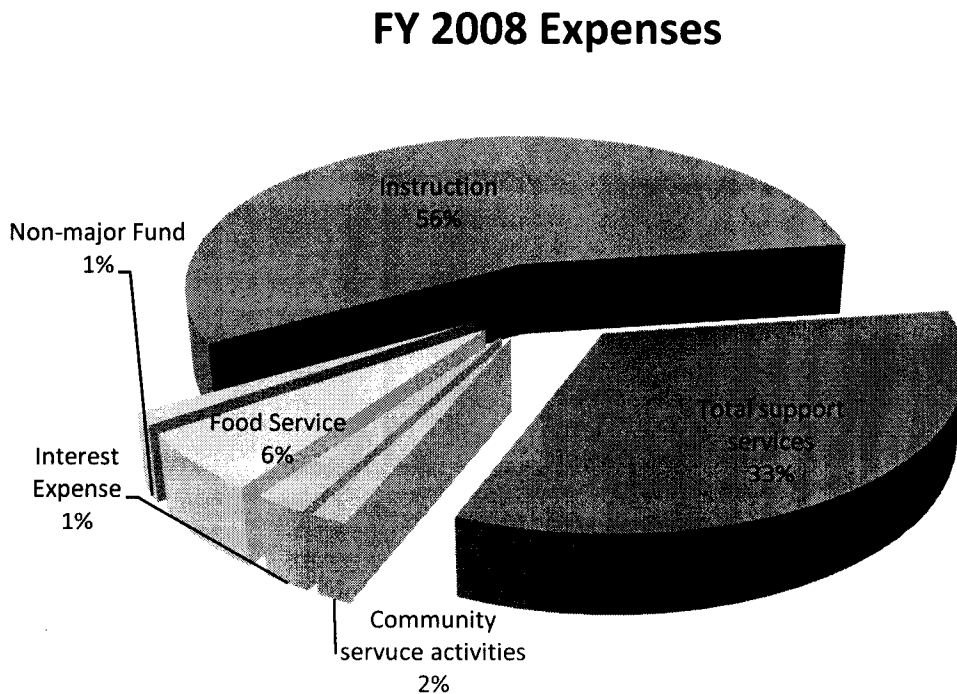
The most significant changes resulted from the following:

- Total local revenue decreased because of a downturn in the economy.
- Operating Grants and Revenues increased because of an increase in grants received.
- Depreciation Expense was allotted to individual expense accounts this year.

District programs for FY 2008 cost \$7.6 million. To support those programs the district garnered \$7.1 million in program revenues. The balance of support came from property taxes and other general revenues. The chart below shows FY 2008 revenues by category.



Instruction comprises 60% of district expenses. Support service expenses make up 30% of the total, with the balance being interest and fiscal charges. The following chart displays FY2008 expenses by category.



Governmental Activities

The *Statement of Activities* on page 13 shows the cost of program services and the charges for services and grants offsetting those services. Table 3 (Net Cost of Services) extract information from the *Statement of Activities* and compares the net cost of services from one year to the next. It identifies the cost of those services supported by tax revenue and unrestricted state entitlements. The net cost of services increased by \$.5 million primarily due to decrease in instruction and interest expense.

Table 3: Net Cost of Services

	June 30, 2007	June 30, 2008	Change	Percentage Change
Instruction	\$ 398,094	\$ 235,424	\$ (162,670)	-41%
Support services				
Student	36,666	14,616	(22,050)	-60%
Instruction staff	50,786	22,120	(28,666)	-56%
District administration	49,233	27,610	(21,623)	-44%
School administration	47,278	22,538	(24,740)	-52%
Business	12,249	5,494	(6,755)	-55%
Plant operation and maintenance	87,148	188,376	101,228	116%
Student transportation	41,413	32,433	(8,980)	-22%
Community service activities	19,786	8,057	(11,729)	-59%
Bond Issuance Cost	4,324	-	(4,324)	100%
Interest Expense	171,946	(134,075)	(306,021)	-178%
<i>Total Expenses</i>	<u>\$ 918,923</u>	<u>\$ 422,593</u>	<u>\$ (496,330)</u>	<u>-54%</u>

The program expense categories shown in Table 3 are summarized below.

- “Instruction” expenses include activities directly dealing with the teaching of pupils and the interaction between teacher and pupil.
- “Instruction-related services” and “pupil services” include the activities involved with assisting staff with the content and process of teaching to pupils, as well as direct non-instructional services to students (including health, library, transportation, and other services).
- “General administration” costs include expenses associated with the administrative and financial supervision of the district.
- “Plant services” involve keeping the school grounds, buildings, and equipment in good working condition.
- “Facilities acquisition and construction” represents the difference between the amount spent on our facilities and the amount capitalized.
- “Interest and fiscal charges” involve the transactions associated with the payment of interest and other charges related to debt of the district.

Financial Analysis of the District's Funds

The district's governmental funds report a combined fund balance of \$1.6 million, which is significantly decreased from last year's total of \$2.4 million. Table 4 (Governmental Fund Balances) provides an analysis of the district's fund balances and the total change in fund balances from the prior year.

Table 4: Governmental Fund Balances

	June 30, 2007	June 30, 2008	Change	Percentage Change
Fund:				
General	\$ 1,429,802	\$ 1,218,530	\$ (211,272)	-15%
Special Revenue	-	-	-	0%
Capital Outlay	4,750	7,572	2,822	0%
Building Fund	2,279	140,914	138,635	6083%
Construction Fund	922,018	241,676	(680,342)	-74%
Debt Service Fund	-	-	-	100%
<i>Total Expenses</i>	<u>\$ 2,358,849</u>	<u>\$ 1,608,692</u>	<u>\$ (750,157)</u>	<u>-32%</u>

The following information helps explain the changes from the prior year.

- Operations
- Construction

General Fund Budgetary Highlights

The district's budget is prepared according to Kentucky law and is based on the modified accrual basis of accounting.

In Kentucky the public school fiscal year is July 1 – June 30; other programs, i.e. some federal programs, operate on a different program calendar, but are reflected in the district overall budget. By Kentucky statute the budget must have a minimum 2% contingency. This district adopted a budget for 2008 and 2009 that satisfies the statute requirement.

We do a draft, tentative and working budget. We made minor amendments the working budget for 2008 based upon unexpected changes in the revenues received or expenditures. The working budget is amended only if there is a significant change in revenues or expenditures. Revenue estimates increased by \$638,644 primarily due to higher than expected SEEK Allotment. Expenditure appropriations increased by \$745,885. Expenditure appropriation adjustments were made to reflect actual staffing, restoration of previously cut programs, increased cost of contracted services, and other changes during the year.

Major differences between final budget amounts and actual revenues and expenditures are identified as follows:

- On behalf adjustment

Capital Assets and Debt Administration

Capital Assets

At the end of the fiscal year, the district had \$12.4 million invested in land, building, equipment (including computer equipment, furniture and vehicles), and construction in progress. Table 5 (Capital Assets) shows FY 2008 balances as compared to FY 2007.

Table 5: Capital Assets

	June 30, 2007	June 30, 2008	Change	Percentage Change
Land	\$ 434,046	\$ 434,046	\$ -	0%
Buildings and improvements	7,577,931	7,577,931	-	0%
Technology Equipment	1,031,473	1,055,607	24,134	2%
Vehicles	437,569	437,569	-	0%
General equipment	231,955	231,955	-	0%
Construction in progress	1,578,198	2,704,942	1,126,744	100%
Total	11,291,172	12,442,050	1,150,878	10%
Less: Accumulated Depreciation	4,425,742	4,650,654	224,912	5%
Net Capital Assets	\$ 6,865,430	\$ 7,791,396	\$ 925,966	13%

In addition we purchased a new vehicles thus accounting for the difference in equipment value, and major construction was in progress on the Middle School renovations for the change in construction in progress. For more information see Note C to the Basic Financial Statements.

Long-Term Debt

At June 30, 2008 the district had \$4.4 million in long term debt obligations. The bulk of this total is debt service on general obligation bonds issued by the district to finance its construction and modernization program. The remaining \$63,917 in long term obligations is the amount of compensated absences liability recorded by the district at year end, a decrease of \$55,275 from the prior year.

Table 6 (Long-Term Debt) shows the district's outstanding debt as of June 30, 2008 as well as comparable data for the prior year. A more detailed discussion is included in Note D to the Basic Financial Statements.

Table 6: Long-Term Debt

	June 30, 2007	June 30, 2008	Change	Percentage Change
General obligation bonds	\$ 4,676,498	\$ 4,381,704	\$ (294,794)	-6%
Compensated absences	119,192	63,917	(55,275)	-46%
Net Capital Assets	\$ 4,795,690	\$ 4,445,621	\$ (350,069)	-7%

Factors bearing on the District's Future

- Attendance percentage.
- Continued decrease of area population.
- Property valuation increases or decreases.
- Economic downturn

Contacting the District's Financial Management

This financial report is designed to provide our citizens, taxpayers, parents, investors and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the money it receives. If you have questions regarding this report or need additional financial information, contact the District's Finance Department at (606) 573-8700 or 420 East Central Street, Harlan, Kentucky 40831.

Harlan Independent School District
Statement of Net Assets - District Wide
As of June 30, 2008

ASSETS	Governmental Activities	Business-type Activities	Total
Current Assets			
Cash and cash equivalents	\$ 1,179,201	\$ 34,116	\$ 1,213,317
Investments	509,121	-	509,121
Accounts receivable			
Taxes	29,370	-	29,370
Intergovernmental - State	26,915	-	26,915
Intergovernmental - Federal	135,465	-	135,465
SFCC	116,389	-	116,389
Inventory	-	7,475	7,475
Total current assets	1,996,461	41,591	2,038,052
Noncurrent Assets			
Capital assets	12,442,050	90,709	12,532,759
Less: Accumulated depreciation	(4,650,654)	(79,976)	(4,730,630)
Total noncurrent assets	7,791,396	10,733	7,802,129
Total assets	\$ 9,787,857	\$ 52,324	\$ 9,840,181
LIABILITIES			
Current Liabilities			
Accounts payable	\$ 129,770	\$ -	\$ 129,770
Accrued payroll and withholding obligations	9,273	-	9,273
Sick leave payable	4,321	-	4,321
Accrued interest payable	50,583	-	50,583
Deferred Revenue	139,648	-	139,648
Current portion of KISTA payable	31,336	-	31,336
Current portion of bonds payable	271,746	-	271,746
Total current liabilities	636,677	-	636,677
Noncurrent Liabilities			
Sick leave payable	59,596	-	59,596
KISTA Payable	126,106	-	126,106
Bonds payable	3,952,516	-	3,952,516
Total noncurrent liabilities	4,138,218	-	4,138,218
Total liabilities	\$ 4,774,895	\$ -	\$ 4,774,895
NET ASSETS			
Invested in capital assets, net of related debt	\$ 3,359,109	\$ 10,733	\$ 3,369,842
Invested in inventory	-	7,475	7,475
Restricted for:			
Encumbrances	12,169	-	12,169
Capital outlay	387,667	-	387,667
Unrestricted	1,254,017	34,116	1,288,133
Total net assets	\$ 5,012,962	\$ 52,324	\$ 5,065,286

The accompanying notes to the financial statements are an integral part of these financial statements.

Harlan Independent School District

Statement of Activities - District Wide

For the year ended June 30, 2008

FUNCTIONS/PROGRAMS

Governmental Activities

	Program Revenues			Net (Expense) Revenue and		
	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-type Activities	Total
Instruction	\$ 4,248,442	\$ -	\$ -	\$ (242,803)	\$ -	\$ (242,803)
Support services	-	-	-	-	-	-
Student	273,495	258,403	-	(15,092)	-	(15,092)
Instruction staff	395,102	372,296	-	(22,806)	-	(22,806)
District administration	441,586	413,215	-	(28,371)	-	(28,371)
School administration	388,961	365,749	-	(23,212)	-	(23,212)
Business	103,154	97,481	-	(5,673)	-	(5,673)
Plant operation and maintenance	739,716	550,326	-	(189,390)	-	(189,390)
Student transportation	181,386	148,679	-	(32,707)	-	(32,707)
Community service activities	111,186	102,940	-	(8,246)	-	(8,246)
Facilities acquisition and construction	-	-	-	-	-	-
Interest Expense	156,248	-	290,323	134,075	-	134,075
Total governmental activities	7,039,276	6,314,727	290,323	(434,226)	-	(434,226)
Business-type Activities						
Food service	431,164	131,439	250,614	-	(1,709)	(1,709)
Non-Major	94,597	71,872	11,803	-	(10,922)	(10,922)
Total business-type activities	525,761	203,311	262,417	-	(12,631)	(12,631)
Total school district	\$ 7,565,037	\$ 203,311	\$ 6,577,144	\$ (434,226)	\$ (12,631)	\$ (446,857)

General Revenues

Ad valorem tax	\$ 471,275	\$ -	\$ 471,275
Sales & use tax	228,136	-	228,136
Other tax	4,348	-	4,348
Tuition	104,665	-	104,665
Earnings on investments	84,307	646	84,953
Other local revenues	15,275	-	15,275
Other revenues	22,282	-	22,282
Gains (Loss) on sale of fixed assets	105	-	105
Total General Revenues	930,393	646	931,039
Change in net assets	496,167	(11,985)	484,182
Net assets - beginning	4,516,795	64,309	4,581,104
Net assets - ending	\$ 5,012,962	\$ 52,324	\$ 5,065,286

The accompanying notes to the financial statements are an integral part of these financial statements.

Harlan Independent School District
Balance Sheet - Governmental Funds
As of June 30, 2008

	General Fund	Special Revenue	Construction Fund	Nonmajor	Total Governmental Funds
ASSETS					
Cash and cash equivalents	\$ 742,850	\$ 13,613	\$ 274,252	\$ 148,486	\$ 1,179,201
Investments	502,057	-	7,064	-	509,121
Accounts receivable					
Taxes	29,370	-	-	-	29,370
Intergovernmental - State	-	26,915	-	-	26,915
Intergovernmental - Federal	-	135,465	-	-	135,465
Total assets	\$ 1,274,277	\$ 175,993	\$ 281,316	\$ 148,486	\$ 1,880,072
Accounts payable	62,733	27,397	39,640	-	129,770
Payroll taxes payable	325	8,948	-	-	9,273
Sick leave payable	4,321	-	-	-	4,321
Deferred revenue	-	139,648	-	-	139,648
Total liabilities	67,379	175,993	39,640	-	283,012
Reserved for:					
Capital outlay	-	-	241,676	145,991	387,667
Unreserved:					
Designated					
Capital projects	444,612	-	-	-	444,612
Undesignated	750,117	-	-	2,495	752,612
Total fund balances	1,206,898	-	241,676	148,486	1,597,060
Total liabilities and fund balances	\$ 1,274,277	\$ 175,993	\$ 281,316	\$ 148,486	\$ 1,880,072

Total fund balances \$ 1,597,060.3

Amounts reported for *governmental activities* in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.	7,791,396
Bond issue costs are not current financial resources and, therefore, are not reported as assets in governmental funds.	-
Accounts receivables for SFCC are not current financial resources and therefore are not reported as revenues in governmental funds.	116,389
Long-term portion of accumulated sick leave is not reported in the governmental fund balance sheet because it is not due and payable in the current period, but it is presented in the statement of net assets.	(59,596)
Interest payable is not reported in the governmental fund balance sheet because it is not due and payable in the current period, but is presented in the statement of net assets.	(50,583)
Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds.	(4,381,704)
Net assets of governmental activities	<u>\$ 5,012,962</u>

The accompanying notes to the financial statements are an integral part of these financial statements.

Harlan Independent School District

Statement of Revenues, Expenditures, and Changes in Fund Balances -

For the year ended June 30, 2008

		Special	Construction		Total
	General Fund	Revenue	Fund	Nonmajor	Governmental
Revenues					Funds
From local sources					
Ad valorem tax	\$ 412,966	\$ -	\$ -	\$ 58,309	\$ 471,275
Sales & use tax	228,136	-	-	-	228,136
Other tax	4,348	-	-	-	4,348
Tuition	48,005	56,660	-	-	104,665
Earnings on investments	58,462	983	22,367	2,495	84,307
Other local revenues	15,358	(83)	-	-	15,275
State sources					
SEEK	3,708,368	-	-	-	3,708,368
Other	3,698	449,229	-	263,309	716,236
Expenditure Reimbursement	11,230	-	-	-	11,230
Revenue in lieu of tax	11,797	-	-	-	11,797
SFCC	-	-	-	290,323	290,323
Federal sources					
Restricted direct	-	181,785	-	-	181,785
Restricted through state	-	692,007	-	-	692,007
Other revenues	1,712	-	-	-	1,712
Total revenues	5,497,384	1,380,581	22,367	614,436	7,514,768
Expenditures					
Instruction	3,179,157	1,059,614	-	-	4,238,771
Support services					
Student	257,436	16,006	-	-	273,442
Instruction staff	234,401	159,563	-	-	393,964
District administration	435,541	1,723	-	-	437,264
School administration	387,036	-	-	-	387,036
Business	90,073	13,081	-	-	103,154
Plant operation and maintenance	541,181	41,175	-	-	582,356
Student transportation	139,719	17,613	-	-	157,332
Community service activities	14,431	94,500	-	-	108,931
Facilities acquisition and construction	-	-	1,126,744	-	1,126,744
Debt Service	-	-	-	487,040	487,040
Total expenditures	5,278,975	1,403,275	1,126,744	487,040	8,296,034
Excess (deficit) of revenues over	218,409	(22,694)	(1,104,377)	127,396	(781,266)
Other Financing Sources (Uses)					
Gain (Loss) on sale of equipment	105	-	-	-	105
Operating transfers in	19,372	55,585	424,035	196,717	695,709
Operating transfers out	(460,790)	(32,891)	-	(182,656)	(676,337)
Total other financing sources:	(441,313)	22,694	424,035	14,061	19,477
Excess (deficit) of revenues and other					
financing sources over expenditures and					
other financing uses	(222,904)	-	(680,342)	141,457	(761,789)
Fund balance, Beginning	1,429,802	-	922,018	7,029	2,358,849
Fund balance, Ending	\$ 1,206,898	\$ -	\$ 241,676	\$ 148,486	\$ 1,597,060

The accompanying notes to the financial statements are an integral part of these financial statements.

Harlan Independent School District

Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balance of Governmental Funds to the Statement of Activities

For the year ended June 30, 2008

Net change in fund balances--total governmental funds	\$ (761,789)
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Amounts reported for governmental activities in the Statement of Activities are different because:

Governmental funds report capital outlays as expenditures. However, in the Statement of Activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which capital outlay exceeded depreciation in the current period.	928,221
Bond issuance costs are current expenditures in the fund financial statements but are increases in assets in the statement of net assets.	-
Bond issuance costs are amortized over the life of the related bonds on the statement of activities	-
Bond and capital lease payments are recognized as expenditures of current financial resources in the governmental fund financial statements, but are reductions of liabilities in the statement of net assets.	317,677
Bond proceeds are recognized as other financing sources and uses in the governmental fund statements but are increases of liabilities in the statement of net assets.	-
Interest payments are recognized as expenditures of current financial resources in the governmental fund financial statements, but are expensed as incurred in the statement of activities.	13,115
Proceeds from the sale of assets are recognized as revenue in the governmental fund financial statements, but only the gain on the sale of assets is recognized as revenue in the statement of activities	-
Accounts receivable for SFCC are not recognized as revenue of current financial resources in the governmental fund financial statements, but are increases of assets in the statement of net assets.	1,198
Changes in non-current sick leave payable are not recognized as expenditures of current financial resources in the governmental fund financial statements, but are reductions or additions of liabilities in the statement of net assets	-

Change in net assets of governmental activities	<u>\$ 498,422</u>
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The accompanying notes to the financial statements are an integral part of these financial statements.

Harlan Independent School District

Statement of Net Assets - Proprietary Funds

As of June 30, 2008

ASSETS	Food Service Fund	Non-major Fund	Total
Current Assets			
Cash and cash equivalents	\$ 34,116	\$ -	\$ 34,116
Inventory	7,475	-	7,475
Total current assets	<u>41,591</u>	<u>-</u>	<u>41,591</u>
Noncurrent Assets			
Furniture and equipment	90,709	-	90,709
Less: Accumulated depreciation	(79,976)	-	(79,976)
Total noncurrent assets	<u>10,733</u>	<u>-</u>	<u>10,733</u>
Total assets	<u>\$ 52,324</u>	<u>\$ -</u>	<u>\$ 52,324</u>
LIABILITIES			
Current Liabilities			
Total current liabilities	<u>-</u>	<u>-</u>	<u>-</u>
Noncurrent Liabilities			
Total noncurrent liabilities	<u>-</u>	<u>-</u>	<u>-</u>
Total liabilities	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
NET ASSETS			
Invested in capital assets, net of related debt	\$ 12,308	\$ -	\$ 12,308
Restricted for:			
Inventory	7,475	-	7,475
Unrestricted	32,541	-	32,541
Total net assets	<u>\$ 52,324</u>	<u>\$ -</u>	<u>\$ 52,324</u>

The accompanying notes to the financial statements are an integral part of these financial statements.

Harlan Independent School District

Statement of Revenues, Expenses, and Changes in Net Assets - Proprietary Funds

For the year ended June 30, 2008

	Food Service Fund	Non-major Fund	Total
Operating Revenues			
Food service sales	\$ 131,405	\$ -	\$ 131,405
Tuition	-	71,875	71,875
Other operating revenues	34	(3)	31
Total operating revenues	<u>131,439</u>	<u>71,872</u>	<u>203,311</u>
Operating Expenses			
Salaries and wages	190,482	96,808	287,290
Professional and contract services	10,073	696	10,769
Supplies and materials	207,593	2,708	210,301
Payments to other funds	19,372	-	19,372
Depreciation	1,575	-	1,575
Other operating expenses	2,069	25	2,094
Total operating expenses	<u>431,164</u>	<u>100,237</u>	<u>531,401</u>
Operating income (loss)	<u>(299,725)</u>	<u>(28,365)</u>	<u>(328,090)</u>
Nonoperating revenues (expenses)			
Federal grants	245,810	-	245,810
State grants	4,804	-	4,804
On-Behalf payments	25,103	11,803	36,906
Commodities Received	22,299	-	22,299
Interest income	646	-	646
Total nonoperating revenues (expenses)	<u>298,662</u>	<u>11,803</u>	<u>310,465</u>
Operating transfers			
Transfers in (out)	<u>-</u>	<u>5,640</u>	<u>5,640</u>
Net income (loss)	<u>(1,063)</u>	<u>(10,922)</u>	<u>(11,985)</u>
Total net assets, beginning	<u>53,387</u>	<u>10,922</u>	<u>64,309</u>
Total net assets, ending	<u>\$ 52,324</u>	<u>\$ -</u>	<u>\$ 52,324</u>

The accompanying notes to the financial statements are an integral part of these financial statements.

Harlan Independent School District

Statement of Cash Flows - Proprietary Funds

For the year ended June 30, 2008

	Food Service Fund	Non-major Fund	Total
Cash Flows from Operating Activities			
Cash received from lunchroom sales	\$ 131,405	\$ -	\$ -
Cash received from other activities	34	77,512	77,546
Cash payments to employees for services	(190,482)	(96,808)	(287,290)
Cash payments to other funds	(19,372)	-	-
Cash payments to suppliers for goods and services	(176,595)	(3,404)	(221,070)
Net cash from operating activities	(257,079)	(22,725)	(432,908)
Cash Flows from Capital Financing Activities			
Acquisition of capital assets	-	-	-
Net cash from capital financing activities	-	-	-
Cash Flows from Noncapital Financing Activities			
Nonoperating grants received	275,717	-	4,804
Net cash from noncapital financing activities	275,717	-	4,804
Cash Flows from Investing Activities			
Interest on investments	646	-	-
Net cash flows from investing activities	646	-	-
Net increase in cash and cash equivalents	19,284	(22,725)	(428,104)
Cash and cash equivalents - beginning	14,832	-	-
Cash and cash equivalents - ending	\$ 34,116	\$ (22,725)	\$ (428,104)
Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities			
Operating income (loss)	\$ (299,725)	\$ (28,365)	\$ (328,090)
Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities			
Depreciation	1,575	-	1,575
Commodities usage	22,299	-	-
Changes in assets and liabilities:			
Accounts receivable	19,383	-	-
Inventory	(611)	-	-
Accounts payable	-	-	-
Net Cash Provided by Operating Activities	\$ (257,079)	\$ (28,365)	\$ (326,515)

The accompanying notes to the financial statements are an integral part of these financial statements.

Harlan Independent School District

Statement of Fiduciary Net Assets - Fiduciary Funds

As of June 30, 2008

ASSETS	<u>Trust/Agency Fund</u>
Current Assets	
Cash and cash equivalents	\$ 124,144
Total current assets	<u>124,144</u>
Noncurrent Assets	
Capital assets	-
Total noncurrent assets	<u>-</u>
Total assets	<u><u>\$ 124,144</u></u>
LIABILITIES	
Current Liabilities	
Due to student groups	\$ 123,144
Total current liabilities	<u>123,144</u>
Noncurrent Liabilities	
Total noncurrent liabilities	<u>-</u>
Total liabilities	<u><u>\$ 123,144</u></u>

The accompanying notes to the financial statements are an integral part of these financial statements.

Harlan Independent School District

Statement of Changes in Fiduciary Net Assets - Fiduciary Funds

For the year ended June 30, 2008

	<u>Trust/Agency Fund</u>
Additions	
Net interest and investment gains (losses)	\$ -
Other additions	422,228
Total additions	<u>422,228</u>
Deductions	
Other deductions	401,629
Total deductions	<u>401,629</u>
Change in net assets	20,599
Net assets - beginning	<u>102,545</u>
Net assets - ending	<u>\$ 123,144</u>

The accompanying notes to the financial statements are an integral part of these financial statements.

Note A – Summary of Significant Accounting Policies

The accounting and reporting framework and the more significant accounting principles and practices of Harlan Independent School District (District) are discussed in subsequent sections of this note. The remainder of the notes are organized to provide explanations, including required disclosures, of the District's financial activities for the fiscal year ended June 30, 2008.

Accounting Principles

The District accounts for its financial transactions in accordance with the policies, procedures, applicable laws and regulations of the State of Kentucky. The accounting policies of the District conform to accounting principles generally accepted in the United States of America as prescribed by the U.S. Governmental Accounting Standards Board ("GASB") and the American Institute of Certified Public Accountants ("AICPA"); and it complies with the requirements of the appropriate version of contracts and grants of agencies from which it receives funds.

Reporting Entity

The District is the level of government primarily accountable for activities related to public education. The governing authority consists of five elected officials whom, together constitute the Board of Education. The District's combined financial statements include the accounts of all its operations. The District evaluated whether any other entity should be included in these financial statements. The basic, but not the only, criterion for including a governmental department, agency, institution, commission, public authority, or other governmental organization in a governmental unit's reporting entity for general purpose financial reports is the ability of the governmental unit's elected officials to exercise over-sight responsibility over such agencies. Oversight responsibility implies that one governmental unit is dependent on another and that the dependent unit should be reported as part of the other. Oversight responsibility is derived from the governmental unit's power and includes, but is not limited to:

- Financial interdependency
- Selection of governing authority
- Designation of management
- Ability to significantly influence operations
- Accountability for fiscal matters

Accordingly, for the year ended June 30, 2008, the District does not have any component units and is not a component unit of any other reporting entity.

Harlan Independent Board of Education Finance Corporation

In a prior year the Board of Education resolved to authorize the establishment of the Harlan Independent School District Finance Corporation (a non-profit, non-stock, public and charitable corporation organized under the School Bond Act and KRS 273 and KRS Section 58.180) (the "Corporation") as an agency for the District for financing the costs of school building facilities. The members of the Board also comprise the Corporation's Board of Directors.

Notes to the Basic Financial Statements – Continued

June 30, 2008

Basis of Presentation

Government-wide Financial Statements:

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the non-fiduciary activities of the District. Eliminations have been made to minimize the effect of interfund activities.

The government-wide statements are prepared using the economic resources measurement focus. This approach differs from the manner in which governmental fund financial statements are prepared. Governmental fund financial statements, therefore, includes a reconciliation with brief explanations to better identify the relationship between the government-wide statements and the statements for the governmental funds.

The government-wide statement of activities presents a comparison between direct expenses and program revenues for each function or program of the District's governmental activities. Direct expenses are those that are specifically associated with a service, program, or department and are therefore clearly identifiable to a particular function. The District does not allocate indirect expenses to functions in the statement of activities. Program revenues include charges paid by the recipients of goods or services offered by a program, as well as grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues are presented as general revenues of the District, with certain exceptions. The comparison of direct expenses with program revenues identifies the extent to which each governmental function is self-financing or draws from the general revenues of the District.

Fund Financial Statements:

Fund financial statements report detailed information about the District. The focus of governmental fund financial statements is on major funds rather than reporting funds by type. Each major governmental fund is presented in a separate column, and all non-major funds are aggregated into one column. Fiduciary funds are reported by fund type.

The accounting and financial treatment applied to a fund is determined by its measurement focus. All governmental funds are accounted for using a flow of current financial resources measurement focus. With this measurement focus, only current assets and current liabilities are generally included on the balance sheet. The Statement of Revenues, Expenditures, and Changes in Fund Balances for these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets.

Agency funds have no measurement focus.

Basis of Accounting

Basis of account refers to when revenues and expenditures are recognized in the accounts and reported in the financial statements. Government-wide financial statements are prepared using the accrual basis of accounting. Governmental funds use the modified accrual basis of accounting. Agency funds use the accrual basis of accounting.

Notes to the Basic Financial Statements – Continued

June 30, 2008

Revenues – Exchange and Non-exchange Transactions:

Revenue resulting from exchange transactions, in which each part gives and receives essentially equal value, is recorded under the accrual basis when the exchange takes place. On the modified accrual basis, revenue is recorded in the fiscal year in which the resources are measurable and become available. “Available” means the resources will be collected with the current fiscal year or are expected to be collected soon enough thereafter to be used to pay liabilities of the current fiscal year. For the District, “available” means collectible within the current period or within 60 days after year-end.

Non-exchange transactions, in which the District receives value without directly giving equal value in return, include property taxes, grants, and entitlements. Under the accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenue from grants and entitlements is recognized in the fiscal year in which all eligibility requirements have been satisfied.

Eligibility requirements include timing requirements, which specify the year when the resources are to be used or the fiscal year when use is first permitted; matching requirement, in which the District must provide local resources to be used for a specific purpose; and expenditure requirements, in which the resources are provided to the District on a reimbursement basis. Under the modified accrual basis, revenue from non-exchange transactions must also be available before it can be recognized.

Deferred revenue:

Deferred revenue arises when assets are received before revenue recognition criteria have been satisfied. Grants and entitlements received before eligibility requirements are met are recorded as deferred revenue. On governmental fund financial statements, receivables associated with nonexchange transactions that will not be collected within the availability period have also been recorded as deferred revenue.

Expenses/Expenditures:

Using the accrual basis of accounting, expenses are recognized at the time a liability is incurred. In the modified accrual basis of accounting, expenditures are generally recognized in the accounting period in which the related fund liability is incurred, as under the accrual basis of accounting. However, under the modified accrual basis of accounting, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due. Allocations of cost, such as depreciation and amortizations, are not recognized in the governmental funds. When both restricted and unrestricted resources are available for use, it is the District’s policy to use restricted resources first, then unrestricted resources as they are needed.

Fund Accounting

The accounts of the District are organized on the basis of funds, each of which is considered to be a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity or retained earnings, revenues, and expenditures or expenses as appropriate. The District’s resources are allocated to and accounted for in individual funds based upon the purpose for which they are to be spent and the means by which spending activities are controlled. The District’s accounts are organized into major, non-major, and fiduciary funds as follows:

Notes to the Basic Financial Statements – Continued

June 30, 2008

Major Governmental Funds:

The General Fund – The general fund is the District's primary operating fund. It accounts for all financial resources except those required to be accounted for in another fund.

Special Revenue Funds – The District accounts for resources restricted to, or designated for, specific purposes by the District or a grantor in a special revenue fund. Most Federal and some State financial assistance is accounted for in a Special Revenue Fund, and sometimes unused balances must be returned to the grantor at the close of specified project periods.

Building Fund – The Facility Support Program of Kentucky (FSPK) accounts for funds generated by the building tax levy required to participate in the School Facilities Construction Commission's construction funding and state matching funds, where applicable. Funds may be used for projects identified in the district's facility plan.

Construction (Capital Projects) Fund – The proceeds from long-term debt financing and revenues and expenditures related to authorized construction and other capital asset acquisitions are accounted for in a capital projects fund.

Non-major Governmental Funds:

Capital Outlay Fund – The Support Education Excellence in Kentucky (SEEK) Capital Outlay Fund receives those funds designated by the state as Capital Outlay Funds and is restricted for use in financing projects identified in the district's facility plan.

Debt Service Funds – The District accounts for resources accumulated and payments made for principal and interest on long-term general obligation debt of governmental funds in a debt service fund.

Fiduciary Funds:

Agency Fund – The District accounts for activities of student groups and others in a custodial capacity in agency funds. These funds are accounted for in accordance with the Uniform Program of Accounting for School Activity Funds.

Proprietary Funds:

The Food Service Fund is used to account for school food service activities, including the National School Lunch Program, which is conducted in cooperation with the U.S. Department of Agriculture (USDA). Amounts have been recorded for in-kind contribution of commodities from the USDA. The Food Service Fund is a major fund.

The Daycare fund is used to account for revenues and expenses related to services provided to daycare services to the surrounding community.

Encumbrances

Encumbrance accounting is used in all budgeted funds to reserve portions of applicable appropriations for which commitments have been made. Encumbrances are recorded for purchase orders, contracts, and other commitments when they are written. Encumbrances are liquidated when the commitments are paid. All encumbrances are liquidated on June 30.

Notes to the Basic Financial Statements – Continued

June 30, 2008

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires the District's Management to make estimates and assumptions that affect reported amounts of assets, liabilities, fund balances, and disclosure of contingent assets and liabilities at the date of the general purpose financial statements, and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

Assets, Liabilities, and Equity

Cash and Investments

Cash balances held in banks and in revolving funds are insured to \$100,000 by the Federal Deposit Insurance Corporation.

The District is authorized to deposit cash and invest excess fund pursuant to the regulations set forth by Kentucky Revised Statute. The funds maintained by the District are either secured by federal depository insurance or are collateralized.

Investments are reported at fair value which is determined using selected bases. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Managed funds are related to the retirement systems not listed on an established market are reported at estimated fair value as determined by the respective fund managers based on quoted sales prices of the underlying securities. Cash deposits are reported at carrying amount which reasonably estimates fair value. Additional cash and investment information, and fair values are presented in Note B.

Inventories and Prepaid Expenditures

Inventories

Inventories are recorded using the purchases method, in that inventory acquisitions are initially recorded as expenditures. Reported inventories are equally offset by a fund balance reserve, which indicates that these amounts are not "available for appropriation and expenditure" even though they are a component of net current assets. The District's inventory is valued at cost and consists of expendable supplies held for consumption.

Prepaid Expenditures

The District has the option of reporting expenditures in governmental funds for prepaid items either when purchased or during the benefiting period. The District has chosen to report the expenditure during the benefiting period, thus recording a prepaid expenditure in the Statement of Net Assets.

Both inventories and prepaids are similarly reported in government-wide and fund financial statements.

Notes to the Basic Financial Statements – Continued

June 30, 2008

Capital Assets

Capital assets are those purchased or acquired with an original cost of \$1,000 or more and are reported at historical cost or estimated historical costs. Contributed assets are reported at fair market value as of the date received. Additions, improvements, and other capital outlays that significantly extend the useful life of an asset are capitalized. The costs of normal maintenance and repairs that do not add to the value of the assets or materially extend the asset's lives are not capitalized, but are expensed as incurred. Depreciation on all capital assets is computed using a straight-line method. When capital assets are disposed, the cost and applicable accumulated depreciation are removed from the respective accounts, and the resulting gain or loss is recorded in operations. Estimated useful lives, in years, for depreciation assets are as follows:

<u>Description</u>	<u>Estimated Useful Lives in Years</u>
Buildings and improvements	25 – 50
Land improvements	20
Technology equipment	5
Vehicles	5 – 10
Audio-visual equipment	15
Food service equipment	10 – 12
Furniture and fixtures	7
Rolling stock	15
Other	10

Deferred Revenue

Cash received for federal and state special project and programs is recognized as revenue to the extent that qualified expenditures have been incurred. Deferred revenue is recorded to the extent that cash received on specific projects and programs exceeds qualified expenditures.

Compensated Absences

Employees are allowed to accrue ten days of sick leave each year without limit. Since the employees' accumulating rights to receive compensation for future absences are contingent upon the absences being caused by future illnesses and such amounts cannot be reasonably estimated, a liability for unused sick leave is not recorded in the financial statements.

Teachers and administrative personnel do not receive paid vacations but are paid only for the number of days they are required to work each year (180 days for teachers and 240 days for administrative personnel).

Maintenance employees are granted vacation leave in varying amounts. In the event of termination an employee is reimbursed for any unused accumulated leave. The District has no liability for unused vacation pay since all vacation leave is used or lost if not taken each year. Vacation pay is charged to operations when taken by the employees of the District.

Upon retirement from the school system, an employee will receive from the District an amount equal to 30% of the value of accumulated sick leave.

Sick leave benefits are accrued as a liability using the termination payment method. An accrual for earned sick leave is made to the extent that it is probable that the benefits will result in termination payments. The liability is based on the School District's past experience of making termination payments.

Notes to the Basic Financial Statements – Continued

June 30, 2008

Long-Term Obligations

In the government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities in the Statement of Net Assets. Bond premiums and discounts as well as issuance costs are deferred and amortized over the life of the bonds using the straight line method. Bonds payable are reported net of applicable bond premium or discount. Bond issuance costs are reported as prepaid expenditures and amortized over the term of the related debt.

In the fund financial statements, governmental funds recognize bond premiums and discounts as well as bond issuance costs during the current period. The face amounts of the debt issued, premiums, or discounts are reported as other financing sources/uses.

Fund Balance Reserves and Designations

Reservations of the ending fund balance indicate the portions of fund balance not appropriable for expenditure or amounts legally segregated for a specific future use. The reserves for revolving fund, inventory, prepaid expenditures, and legally restricted balances reflect the portions of fund balance represented by each respective account. These amounts are not available for appropriation and expenditure at the balance sheet date.

Designations of the ending fund balance indicate tentative plans for financial resource utilization in a future period.

Net Assets

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets net of related debt consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowings used for the acquisition, construction or improvement of those assets. Net assets are reported as restricted when there are limitation imposed on their use either through the enabling legislation adopted by the District or through external restrictions imposed by creditors, grantors, laws or regulations of other governments. The District applies restricted resources when an expense is incurred for purposed for which both restricted and unrestricted net assets are available.

Revenue Limit/Property Tax

The District's revenue limit is received from a combination of local property taxes, state apportionments, and other local sources.

The county is responsible for assessing, collecting, and apportioning property taxes. Taxes are levied for each fiscal year on taxable real and personal property in the county. The levy is based on the assessed values as of the preceding January 1, which is also the lien date. Property taxes on the secured roll are due on November 1, and become delinquent February 1. Property tax revenues are considered available (1) when they become due or past due and receivable within the current period and (2) when they are expected to be collected during a 60-day period after the close of the school fiscal year. The assessed value of the certified roll, upon which the levy for the 2007 fiscal year was based upon, was in excess of \$90.8 million.

Taxes are due on November 1 and become delinquent by February 1 following the October 1 levy date. Current tax collections for the year ended June 30, 2008 were 93% of the tax levy.

The property tax rates assessed for the year ended June 30, 2008, to finance the General Fund operations were \$.387 per \$100 valuation for real property, \$.430 per \$100 valuation for business personal property, and \$.523 per \$100 valuation for motor vehicles.

Notes to the Basic Financial Statements – Continued

June 30, 2008

The District levies a utility gross receipts license tax in the amount of 3% of the gross receipts derived from the furnishing, within the county, of telephonic and telegraphic communications services, cablevision services, electric power, water, and natural, artificial and mixed gas.

Risk Management

The district is exposed to various risk of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. To obtain insurance for workers' compensation, errors and omissions, and general liability coverage, the District purchases insurance coverage, from a private insurance agent, through a cooperative on a competitive bidding basis.

The District purchases unemployment insurance through the Kentucky School Boards Insurance Trust Unemployment Compensation Fund; however, risk has not been transferred to such fund. In addition, the District continues to carry commercial insurance for all other risks of loss.

There were no significant reductions in insurance coverage in the current fiscal year. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

Interfund Transactions

Interfund transactions are reported as either loans, services provided, reimbursements, or transfers. Loans are reported as interfund receivable and payable, as appropriate and are subject to elimination upon consolidation. Services provided, deemed to be at market or near market rates, are treated as revenues and expenditures/expenses. Reimbursements occur when one fund incurs a cost, charges the appropriate benefiting fund, and reduces its related cost as a reimbursement. All other interfund transactions are treated as transfers. Transfers among governmental funds are eliminated in the government-wide financial statements.

Note B – Cash and Investments

For discussion of adopted deposit and investment policy and other related information, see Note A.

Deposits

Custodial credit risk for deposits is the risk that in the event of a bank failure, the District's deposits may not be returned or the District will not be able to recover collateral securities in the possession of an outside party. The District's policy requires deposits to be 100 percent secured by collateral valued at market or par, whichever is lower, less the amount covered by the Federal Deposit Insurance Corporation (FDIC). Deposited funds may be invested in certificates of deposit in institutions with an established record of fiscal health and service, as determined by a rating of C minus or above by independent rating agencies. Collateral agreements must be approved prior to deposit of funds as provided by law. The District council approves and designates a list of authorized depository institutions based on evaluation of solicited responses and certifications provided by financial institutions and recommendations of an evaluation committee or the District treasurer, or both. **Custodial credit risk** for deposits is not formally addressed by bond indentures or pension trust policy. Indentures require that restricted deposits be maintained by the trustee bank specified in the indenture. Pension trust investment policy restricts uninvested cash to minimal balances generally covered by the FDIC.

Deposits of the District's reporting entity are insured or collateralized with securities held by the District, its agent, or by the pledging financial institution's trust department or agent in the name of the District or applicable public trust.

Notes to the Basic Financial Statements – Continued

June 30, 2008

Note C – Capital Assets

Capital asset activity for the fiscal year ended June 30, 2008, was as follows:

<u>Governmental Activities</u>	Balance July 1, 2007	Additions	Deductions	Balance June 30, 2008
Land	\$ 434,046	\$ -	\$ -	\$ 434,046
Buildings and improvements	7,577,931	-	-	7,577,931
Technology Equipment	1,031,473	24,134	-	1,055,607
Vehicles	437,569	-	-	437,569
General equipment	231,955	-	-	231,955
Construction in progress	1,578,198	-	-	1,578,198
Totals at historical cost	<u>11,291,172</u>	<u>24,134</u>	<u>-</u>	<u>11,315,306</u>
Less: accumulated depreciation				
Buildings and improvements	3,027,949	150,307	-	3,178,256
Technology Equipment	905,532	37,507	-	943,039
Vehicles	320,455	23,917	-	344,372
General equipment	171,806	13,181	-	184,987
Total accumulated depreciation	<u>4,425,742</u>	<u>224,912</u>	<u>-</u>	<u>4,650,654</u>
Governmental Activities Capital Assets - Net	<u>\$ 6,865,430</u>	<u>\$ (200,778)</u>	<u>\$ -</u>	<u>\$ 6,664,652</u>
<u>Business-Type Activities</u>				
Food service and equipment	\$ 90,709	\$ -	\$ -	\$ 90,709
Totals at historical cost	<u>90,709</u>	<u>-</u>	<u>-</u>	<u>90,709</u>
Less: accumulated depreciation				
Food service and equipment	78,401	1,575	-	79,976
Total accumulated depreciation	<u>78,401</u>	<u>1,575</u>	<u>-</u>	<u>79,976</u>
Business-Type Activities Capital Assets - Net	<u>\$ 12,308</u>	<u>\$ (1,575)</u>	<u>\$ -</u>	<u>\$ 10,733</u>

Depreciation expense was charged to governmental activities as follows:

<u>Governmental Activities Depreciation Expense by Function</u>	
Instruction	\$ 33,805
Support services	
Student	53
Instruction staff	1,138
District administration	4,322
School administration	1,925
Plant operation and maintenance	157,360
Student transportation	24,054
Community services	2,255
	<u>\$ 224,912</u>

Notes to the Basic Financial Statements – Continued

June 30, 2008

Note D – Bonded Debt

The original amount of each issue, the issue date, and interest rates and summary of changes are summarized below:

Maturity	Interest Rates	Original Issue	Principal Balance 7/1/2007	Debt Issued	Debt Paid	Principal Balance 6/30/2008	Due Within One Year
Apr-13	?	?	\$ 15,040	\$ -	\$ 2,960	\$ 12,080	\$ 2,980
Mar-20	3.70% to 5.375%	2,240,000	1,760,000	-	80,000	1,680,000	85,000
May-15	3.00% to 3.70%	1,005,000	860,000	-	75,000	785,000	80,000
Aug-26	3.80% to 4.40%	1,643,000	1,643,000	-	56,000	1,587,000	58,000
Nov-11	0%	228,831	205,948	-	45,766	160,182	45,766
Mar-08	4.00% to 4.60%	\$ 69,852	\$ 5,673	\$ -	\$ 5,673	\$ -	\$ -
Mar-08	3.50% to 4.20%	70,144	11,175	-	5,503	5,672	5,672
Mar-11	4.15% to 4.60%	78,191	25,985	-	6,671	19,314	6,942
Mar-13	2.00% to 3.90%	66,768	33,597	-	5,525	28,072	5,674
Mar-15	3.00% to 3.625%	62,504	49,326	-	5,800	43,526	5,981
Mar-17	3.50% to 3.875%	66,754	66,754	-	5,896	60,858	7,067
			119,192			119,192	-
					\$ 4,500,896	\$ 303,082	

Payments on the General Obligation Bonds are made from the Debt Service Fund using local revenues and SFCC Contributions. Compensated absences are paid by the general fund.

In connection with the school revenue bonds issued after May 1, 1989 the District entered into "participation agreements" with the School Facility Construction Commission. The Commission was created by the Kentucky General Assembly for the purpose of assisting local school districts in meeting school construction needs. The table below sets forth the amount to be paid by the District and the Commission for each year until maturity of all bond issues. The liability for the total bond amount remains with the District and, as such, to total principal outstanding has been recorded in the financial statements.

The bonds may be called prior to maturity and redemption premiums are specified in each issue. Assuming no bonds are called prior to scheduled maturity, the minimum obligation of the District, including amounts to be paid by the Commission, at June 30, 2008 for debt service (principal and interest) are as follows:

Notes to the Basic Financial Statements – Continued

June 30, 2008

Fiscal Year Ending June 30,	SFCC		District		Total
	Interest	Principal	Interest	Principal	
2009	\$ 116,626	\$ 173,733	\$ 61,065	\$ 98,013	\$ 449,438
2010	109,972	180,328	58,727	98,423	447,450
2011	102,815	187,538	56,807	137,718	484,878
2012	95,289	195,027	52,117	122,482	464,915
2013	87,396	202,994	47,732	95,006	433,128
2014 - 2018	313,008	848,770	160,940	582,230	1,904,948
2019 - 2023	149,388	586,318	16,645	293,682	1,046,034
2024 - 2028	35,536	418,918	271	3,082	457,807
	<u>\$ 1,010,030</u>	<u>\$ 2,793,626</u>	<u>\$ 454,304</u>	<u>\$ 1,430,636</u>	<u>\$ 5,688,596</u>

KISTA Bonds:

Fiscal Year Ending June 30,	District Interest	Principal	Total
2009	\$ 5,778	\$ 31,336	\$ 37,114
2010	4,630	24,153	28,783
2011	3,755	25,078	28,833
2012	2,817	18,312	21,129
2013	2,156	19,014	21,170
2014 - 2018	3,221	39,549	42,770
	<u>\$ 22,357</u>	<u>\$ 157,442</u>	<u>\$ 179,799</u>

Note E – Lease Obligations

The District was not entered into any material capital or operating leases as of June 30, 2008

Note F – Retirement Plans

The payroll for employees covered under the following plans are as follows:

The Teachers' Retirement Systems

Plan Description – The Harlan Independent School System contributes to the Teachers' Retirement System of Kentucky (KTRS), a cost sharing, multiple employer defined benefit pension plan. KTRS administers retirement and disability annuities, and death and survivor benefits to employees and beneficiaries of employees of the public school systems and other public educational agencies in Kentucky.

KTRS was created by the 1938 General Assembly and is governed by Chapter 161 Section 220 through Chapter 161 Section 990 of the *Kentucky Revised Statutes* (KRS). KTRS issues a publicly available financial report that includes financial statements and required supplementary information for the defined benefit pension plan. That report can be obtained by writing to Kentucky Teachers' Retirement System, 479 Versailles Road, Frankfort, Kentucky 40601.

Notes to the Basic Financial Statements – Continued

June 30, 2008

Funding Policy – Contribution rates are established by KRS. Members are required to contribute 9.855% of their salaries to KTRS. The Commonwealth of Kentucky is required to contribute 13.105% of salaries. The federal program for any salaries paid by that program pays the matching contributions. KTRS requires that members of KTRS occupy a position requiring either a four (4) year college degree or certification by Kentucky Department of Education (KDE).

The Harlan Independent School System's total payroll for the year was \$4,366,443. The payroll for employees covered under KTRS was \$3,396,586. For the year ended June 30, 2008, the Commonwealth contributed \$1,211,164 in matching to KTRS for the benefit of our participating employees. The School District's contributions to KTRS for the year ending June 30, 2008 were \$216,003, which represents those employees covered by federal programs.

County Employees Retirement System

Employees who work an average of 100 hours per month participate in the County Employees Retirement System of Kentucky (CERS) which is a cost sharing, multiple-employer public employees retirement system created by and operating under Kentucky law. The County Employees Retirement System covers substantially all regular non-certified full-time employees of each county and school board, and any additional local agencies electing to participate. The plan provides for retirement, disability and death benefits. CERS issues a publicly available financial report that includes financial statement and required supplementary information. The report may be obtained in writing from the County Employee Retirement System, 1260 Louisville Road, Perimeter Park West, Frankfort, Kentucky 40601.

Participating employees contribute 5% of the creditable compensation. Employer contribution rates are intended to fund the normal cost of a current basis plus on percent (1%) of unfounded past service costs per annum plus interest at the actuarial assumed rate. Such contribution rates are determined by the Board of Trustees of Kentucky Retirement Systems each biennium. The Board contributed \$223,376 of the employee's compensation during the fiscal year ended June 30, 2008. The Board's required contribution (both withholding and match) for pension obligations to CERS for the fiscal year ended June 30, 2008 has been contributed for the fiscal year.

Note G – Deficit Operating / Fund Balances

There are no funds of the District that currently have a deficit fund balance. However, the following funds have operations that resulted in a current year deficit of revenues over expenditures resulting in a corresponding reduction of fund balance:

General Fund	<\$ 211,272>
Construction Fund	<\$ 680,242>
Food Service Fund	<\$ 1,063>
Non-major Proprietary Fund	<\$ 10,922>

Note H – Transfer of Funds

Transfers and payments within the reporting entity are substantially for the purposes of subsidizing operating functions, funding capital projects and asset acquisitions, or maintaining debt service on a routine basis. Resources are accumulated in a fund or component unit to support and simplify the administration of various projects or programs.

The government-wide statement of activities eliminates transfers reported within the segregated governmental and business-type activities columns. Only transfers *between* the two columns appear in this statement.

The following schedule reports transfers and payments within the reporting entity:

Notes to the Basic Financial Statements – Continued

June 30, 2008

For	From Fund	Amount	To Fund	Amount
Debt Service Payments	General Fund	\$ 460,790	Debt Service Fund	\$ 43,061
Construction			Construction Fund	\$ 367,784
Matching			Special Revenue Fund	\$ 49,945
Construction	Special Revenue Fund	68,698	Construction Fund	27,251
Interproject Transfers			Special Revenue Fund	29,815
Indirect Cost			General Fund	11,632
Debt Service Payments	Capital Outlay Fund		Debt Service Fund	
Debt Service Payments	Non-Major Fund	182,656	Debt Service Fund	153,656
Construction			Construction Fund	29,000
Indirect Cost	Food Service Fund	19,372	General Fund	19,372

Note I – Commitments and Contingencies**Grant Programs**

In the normal course of operations, the District received grant funds from various Federal and state agencies. The grant programs are subject to audit by agents of the granting authorities the purpose of which is to ensure compliance with conditions precedent to the granting of funds. Any liability for reimbursement which may arise as the result of these audits is not believed to be material.

Litigation

The District is party to various legal proceedings which normally occur in governmental operations. These legal proceedings are not likely to have a material adverse impact on the affected funds of the District.

Future Construction

As of June 30, 2008 a new preschool building was beginning.

COBRA

Under COBRA, employers are mandated to notify terminated employees of available continuing insurance coverage. Failure to comply with this requirement may put the school district at risk for a substantial loss (contingency).

Note J – On-Behalf Payments

The State of Kentucky makes certain health insurance, life insurance, flexible spending, administrative fees and pension plan payments on behalf of the District for its employees. The District records these payments as both a revenue and expenditure in the General Fund and Food Service Fund based upon percentage of payroll. The total of the on-behalf payments for the fiscal year ended June 30, 2008 was \$.993 million for the General Fund and \$25,103 for the Food Service Fund. The District is not legally responsible for these contributions.

Required Supplemental Information

Budgetary Comparison Schedules

Required Supplementary Information

For the year ended June 30, 2008

General Fund						
	Budgeted Amounts		Actual GAAP Basis	Adjustments Budget Basis	Actual Budget Basis	Variance with Final Budget Favorable (Unfavorable)
Revenues	Original	Final				
From local sources						
Ad valorem tax	\$ 400,100	\$ 400,000	\$ 412,966	\$ -	\$ 412,966	\$ 12,966
Sales & use tax	180,000	200,000	228,136	-	228,136	28,136
Other tax	5,000	3,000	4,348	-	4,348	1,348
Tuition	75,000	25,000	48,005	-	48,005	23,005
Earnings on investments	48,000	50,000	58,462	-	58,462	8,462
Other local revenues	6,500	10,300	15,358	-	15,358	5,058
State sources					-	
SEEK	2,910,056	3,560,000	3,708,368	-	3,708,368	148,368
Other	4,000	9,000	3,698	-	3,698	(5,302)
Expenditure Reimbursements	8,000	8,000	11,230	-	11,230	3,230
Revenue in lieu of tax	-	10,000	11,797	-	11,797	1,797
On behalf payments	-	-	993,304	(993,304)	-	-
Other revenues	-	-	1,712	-	1,712	1,712
Total revenues	3,636,656	4,275,300	5,497,384	(993,304)	4,504,080	228,780
Expenditures						
Instruction	2,224,759	2,508,729	3,179,157	(706,032)	2,473,125	35,604
Support services						
Student	222,712	247,049	257,436	(47,552)	209,884	37,165
Instruction staff	149,832	199,067	234,401	(41,667)	192,734	6,333
District administration	667,195	905,637	435,541	(32,199)	403,342	502,295
School administration	263,724	305,696	387,036	(83,899)	303,137	2,559
Business	74,629	84,071	90,073	(14,763)	75,310	8,761
Plant operation and maintenance	455,702	531,722	541,181	(45,346)	495,835	35,887
Student transportation	116,600	130,841	139,719	(21,846)	117,873	12,968
Central office	-	-	-	-	-	-
Community service activities	19,478	20,668	14,431	-	14,431	6,237
Debt Service	36,025	43,061	-	-	-	43,061
Total expenditures	4,230,656	4,976,541	5,278,975	(993,304)	4,285,671	690,870
Excess (deficit) of revenues over expenditures	(594,000)	(701,241)	218,409	-	218,409	919,650
Other Financing Sources (Uses)						
Proceeds of long-term capital-related debt	-	34,206	-	-	-	(34,206)
Gain (Loss) on sale of equipment	-	-	105	-	105	105
Operating transfers in	20,000	24,000	19,372	-	19,372	(4,628)
Operating transfers out	(26,000)	(15,000)	(460,790)	-	(460,790)	(445,790)
Total other financing sources (uses)	(6,000)	43,206	(441,313)	-	(441,313)	(484,519)
Excess (deficit) of revenues and other financing sources over expenditures and other financing uses	(600,000)	(658,035)	(222,904)	-	(222,904)	435,131
Fund balance, beginning	600,000	658,035	1,429,802	-	1,429,802	771,767
Fund balance, ending	\$ -	\$ -	\$ 1,206,898	\$ -	\$ 1,206,898	\$ 1,206,898

The accompanying notes to the required supplementary schedules are an integral part of these financial statements.

Harlan Independent School District

Budgetary Comparison Schedules

Required Supplementary Information

For the year ended June 30, 2008

	Special Revenue Fund					Variance
	Budgeted Amounts		Actual	Adjustments	Actual	Budget
Revenues	Original	Final	GAAP Basis	Budget Basis	Budget Basis	Favorable Unfavorable
From local sources						
Tuition	\$ -	\$ -	\$ 56,660	\$ -	\$ 56,660	\$ 56,660
Earnings on investments	2,285	43	983	-	983	940
Other local revenues	-	-	(83)	-	(83)	(83)
State sources						
Other	1,531,552	545,634	449,229	-	449,229	(96,405)
On behalf payments	-	(28,480)	-	-	-	28,480
Federal sources						
Restricted direct	-	-	181,785	-	181,785	181,785
Ristricted throught state	1,670,668	556,065	692,007	-	692,007	135,942
Total revenues	3,204,505	1,073,262	1,380,581	-	1,380,581	307,319
Expenditures						
Instruction	2,655,434	890,366	1,059,614	-	1,059,614	(169,248)
Support services						
Student	22,751	4,025	16,006	-	16,006	(11,981)
Instruction staff	225,558	76,869	159,563	-	159,563	(82,694)
District administration	-	-	1,723	-	1,723	(1,723)
School administration	(1,316)	(1,316)	-	-	-	(1,316)
Business	38,453	16,525	13,081	-	13,081	3,444
Plant operation and maintenance	-	-	41,175	-	41,175	(41,175)
Student transportation	36,764	12,833	17,613	-	17,613	(4,780)
Community service activities	290,876	94,500	94,500	-	94,500	-
Total expenditures	3,268,520	1,093,802	1,403,275	-	1,403,275	(309,473)
Excess (deficit) of revenues over expenditures	(64,015)	(20,540)	(22,694)	-	(22,694)	(2,154)
Other Financing Sources (Uses)						
Operating transfers in	58,825	17,054	55,585	-	55,585	38,531
Operating transfers out	-	-	(32,891)	-	(32,891)	(32,891)
Total other financing sources (uses)	58,825	17,054	22,694	-	22,694	5,640
Excess (deficit) of revenues and other financing sources over expenditures and other financing uses	(5,190)	(3,486)	-	-	-	3,486
Fund balance, beginning	34,905	34,905	-	-	-	(34,905)
Fund balance, ending	\$ 29,715	\$ 31,419	\$ -	\$ -	\$ -	\$ (31,419)

The accompanying notes to the required supplementary schedules are an integral part of these financial statements.

Harlan Independent School District
Budgetary Comparison Schedules
 Required Supplementary Information
 For the year ended June 30, 2008

	Construction Fund					Variance Budget Favorable (Unfavorable)
	Budgeted Amounts		Actual GAAP Basis	Adjustments Budget Basis	Actual Budget Basis	
	Original	Final				
Revenues						
From local sources						
Earnings on investments	\$ 45,000	\$ 8,031	\$ 22,367	\$ -	\$ 22,367	\$ 14,336
Other local revenues	313,000	311,271	-	-	-	(311,271)
Total revenues	358,000	319,302	22,367	-	22,367	(296,935)
Expenditures						
Support services						
Plant operation and maintenance	-	446	-	-	-	446
Facilities acquisition and construction	3,126,830	1,652,156	1,126,744	-	1,126,744	525,412
Total expenditures	3,126,830	1,652,602	1,126,744	-	1,126,744	525,858
Excess (deficit) of revenues over expendi	(2,768,830)	(1,333,300)	(1,104,377)	-	(1,104,377)	228,923
Other Financing Sources (Uses)						
Proceeds of long-term capital-related d	1,651,000	8,000	-	-	-	(8,000)
Operating transfers in	965,831	415,689	424,035	-	424,035	8,346
Total other financing sources (uses)	2,616,831	423,689	424,035	-	424,035	346
Excess (deficit) of revenues and other financing sources over expenditures and other financing uses	(151,999)	(909,611)	(680,342)	-	(680,342)	229,269
Fund balance, beginning	-	-	922,018	-	922,018	922,018
Fund balance, ending	\$ (151,999)	\$ (909,611)	\$ 241,676	\$ -	\$ 241,676	\$ 1,151,287

The accompanying notes to the other supplementary schedules are an integral part of these financial statements.

Note A – Budgets and Budgetary Accounting

Budget Policy and Practice

The district's budget is prepared according to Kentucky law and is based on the modified accrual basis of accounting. The budget is presented to the District board for review. In June, the District council adopts the annual fiscal year budgets for District operating funds. Once approved, the District council may amend the legally adopted budget when unexpected modifications are required in estimated revenues and appropriations. Special Revenue funds are budgeted on a project-length basis and are also subjected to the council review and approval process. By state law, the District's board must adopt a final budget no later than July 1. The District's board satisfied these requirements.

These budgets are revised by the District's governing board during the year to give consideration to unanticipated income and expenditures. The original and final revised budgets for the General Fund and Special Revenue Fund are presented as Required Supplementary Information. The General Fund's final budgeted expenditures increased by \$ 450,281 from the original budget. The changes from original to final budgets were not material in other funds.

Basis of Budgeting

Revenues are budgeted by source. Expenditures are budgeted by department and class as follows: Instruction, Support Services, Community Service Activities, Facilities Acquisition and Construction and Debt Service. Budget revisions at this level are managed administratively and reported to the District board. The legal level of control is by department within a fund. Expenditures may not exceed appropriations at this level. Within these control levels, management may transfer appropriations without council approval. Revisions to the budget were made throughout the year.

The budgets for the operating funds and proprietary fund operations are prepared on a basis consistent with generally accepted accounting principles for all government funds, except for the Debt Service Fund. A legally adopted budget is not required for this fund. The budget and actual financial statements are reported on these bases. Unencumbered appropriations for annually budgeted funds lapse at fiscal year-end.

Note B – Excess of Expenditures over Appropriations

The District did not budget appropriations, in the General Fund, for on-behalf payments provided by the Kentucky Department of Education because they were not measurable at the time of budgeting. Therefore, these expenditures were adjusted out of the actual basis to mirror actual budget basis for review.

As of June 30, 2008, expenditures exceeded appropriation in individual funds as follows:

Notes to the Required Supplementary Information - Continued

June 30, 2008

Appropriations Category	Excess Expenditures	Explanation
Special Revenue Fund		
Instruction	\$ 169,248	Salary reclassification
Support services		
Student	11,981	Salary reclassification
		Budgetary process of project budgeting. The entire budget is in the first year of the project and all expenditures after that are "unbudgeted" because of timing.
Instruction staff	82,694	Budgetary process of project budgeting. The entire budget is in the first year of the project and all expenditures after that are "unbudgeted" because of timing.
District administration	1,723	Budgetary process of project budgeting. The entire budget is in the first year of the project and all expenditures after that are "unbudgeted" because of timing.
School administration	1,316	Budgetary process of project budgeting. The entire budget is in the first year of the project and all expenditures after that are "unbudgeted" because of timing.
Plant operation and maintenance	41,175	Budgetary process of project budgeting. The entire budget is in the first year of the project and all expenditures after that are "unbudgeted" because of timing.
Student transportation	4,780	Budgetary process of project budgeting. The entire budget is in the first year of the project and all expenditures after that are "unbudgeted" because of timing.

Other Supplemental Information

Harlan Independent School District

Combining Balance Sheet - Nonmajor Governmental Funds

For the year ended June 30, 2008

	Capital Outlay Fund	Building	Debt Service Fund
ASSETS			
Cash and cash equivalents	\$ 7,572	\$ 140,914	\$ -
Total assets	<u>\$ 7,572</u>	<u>\$ 140,914</u>	<u>\$ -</u>
LIABILITIES AND FUND BALANCES			
Liabilities			
Total liabilities	<u>-</u>	<u>-</u>	<u>-</u>
Fund Balances			
Reserved for:			
Capital Outlay	6,834	139,157	-
Unreserved:			
Undesignated	738	1,757	-
Total fund balances	<u>7,572</u>	<u>140,914</u>	<u>-</u>
Total liabilities and fund balances	<u>\$ 7,572</u>	<u>\$ 140,914</u>	<u>\$ -</u>

The accompanying notes to the supplementary schedules are an integral part of these financial statements.

Total
Governmental
Funds

\$	148,486
\$	148,486

	-

145,991

	2,495
	148,486
\$	148,486

The accompanying notes to the supplementary schedules are an integral part of these financial statements.

Harlan Independent School District

Combining Balance Sheet - Nonmajor Governmental Funds

For the year ended June 30, 2008

	Capital Outlay Fund	Building	Debt Service Fund	Total Governmental Funds
ASSETS				
Cash and cash equivalents	\$ 7,572	\$ 140,914	\$ -	\$ 148,486
Total assets	<u>\$ 7,572</u>	<u>\$ 140,914</u>	<u>\$ -</u>	<u>\$ 148,486</u>
LIABILITIES AND FUND BALANCES				
Liabilities				
Total liabilities	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Fund Balances				
Reserved for:				
Capital Outlay	6,834	139,157	-	145,991
Unreserved:				
Undesignated	738	1,757	-	2,495
Total fund balances	<u>7,572</u>	<u>140,914</u>	<u>-</u>	<u>148,486</u>
Total liabilities and fund balances	<u>\$ 7,572</u>	<u>\$ 140,914</u>	<u>\$ -</u>	<u>\$ 148,486</u>

The accompanying notes to the supplementary schedules are an integral part of these financial statements.

Harlan Independent School District

Combining Statement of Revenues, Expenditures, and Changes in Fund Balance - Nonmajor

For the year ended June 30, 2008

	Capital Outlay Fund	Building Fund	Debt Service Fund	Total Nonmajor Funds
Revenues				
From local sources				
Ad valorem tax	\$ -	\$ 58,309	\$ -	\$ 58,309
Earnings on investments	738	1,757	-	2,495
State sources				
Other	76,850	186,459	-	263,309
SFCC	-	-	290,323	290,323
Total revenues	<u>77,588</u>	<u>246,525</u>	<u>290,323</u>	<u>614,436</u>
Expenditures				
Debt Service	-	-	487,040	487,040
Total expenditures	<u>-</u>	<u>-</u>	<u>487,040</u>	<u>487,040</u>
Excess (deficit) of revenues over expenditures	<u>77,588</u>	<u>246,525</u>	<u>(196,717)</u>	<u>127,396</u>
Other Financing Sources (Uses)				
Operating transfers in	-	-	196,717	196,717
Operating transfers out	(74,766)	(107,890)	-	(182,656)
Total other financing sources (uses)	<u>(74,766)</u>	<u>(107,890)</u>	<u>196,717</u>	<u>14,061</u>
Excess (deficit) of revenues and other financing sources over expenditures and other financing uses	<u>2,822</u>	<u>138,635</u>	<u>-</u>	<u>141,457</u>
Fund balance, beginning	<u>4,750</u>	<u>2,279</u>	<u>-</u>	<u>7,029</u>
Fund balance, ending	<u><u>\$ 7,572</u></u>	<u><u>\$ 140,914</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 148,486</u></u>

The accompanying notes to the supplementary schedules are an integral part of these financial statements.

Harlan Independent School District

Combining Statement of Net Assets - Nonmajor Proprietary Funds

For the year ended June 30, 2008

	Sunshine Daycare Fund	Total
ASSETS		
Current Assets		
Total current assets	<u>-</u>	<u>-</u>
Noncurrent Assets		
Total noncurrent assets	<u>-</u>	<u>-</u>
Total assets	<u><u>\$ -</u></u>	<u><u>\$ -</u></u>
LIABILITIES		
Current Liabilities		
Total current liabilities	<u>-</u>	<u>-</u>
Noncurrent Liabilities		
Total noncurrent liabilities	<u>-</u>	<u>-</u>
Total liabilities	<u><u>\$ -</u></u>	<u><u>\$ -</u></u>
NET ASSETS		
Total net assets	<u><u>\$ -</u></u>	<u><u>\$ -</u></u>

The accompanying notes to the supplementary schedules are an integral part of these financial statements.

Harlan Independent School District

Combining Statement of Revenues, Expenses, and Changes in Net Assets - Nonmajor Proprietary Funds

For the year ended June 30, 2008

	Sunshine Daycare Fund	Total
Operating Revenues		
Tuition	\$ 71,875	\$ 71,875
Other operating revenues	(3)	(3)
Total operating revenues	<u>71,872</u>	<u>71,872</u>
Operating Expenses		
Salaries and wages	96,808	96,808
Professional and contract services	696	696
Supplies and materials	2,708	2,708
Other operating expenses	25	25
Total operating expenses	<u>100,237</u>	<u>100,237</u>
Operating income (loss)	<u>(28,365)</u>	<u>(28,365)</u>
Nonoperating revenues (expenses)		
Total nonoperating revenues (expenses)	<u>11,803</u>	<u>11,803</u>
Operating transfers		
Transfers in (out)	<u>5,640</u>	<u>5,640</u>
Net income (loss)	<u>(10,922)</u>	<u>(10,922)</u>
Total net assets, beginning	<u>10,922</u>	<u>10,922</u>
Total net assets, ending	<u>\$ -</u>	<u>\$ -</u>

The accompanying notes to the supplementary schedules are an integral part of these financial statements.

Harlan Independent School District
Budgetary Comparison Schedules
Other Supplementary Information
For the year ended June 30, 2008

	Capital Outlay Fund				Variance
	Budgeted Amounts		Actual	Adjustments	Budget
	Original	Final	GAAP	Budget	Favorable
			Basis	Basis	(Unfavorable)
Revenues					
From local sources					
Earnings on investments	\$ -	\$ -	\$ 738	\$ -	\$ 738
State sources					
Other	66,710	74,630	76,850	-	2,220
Total revenues	<u>66,710</u>	<u>74,630</u>	<u>77,588</u>	<u>-</u>	<u>2,958</u>
Expenditures					
Facilities acquisition and constructio	141,240	49,630	-	-	49,630
Debt Service	-	25,000	-	-	25,000
Total expenditures	<u>141,240</u>	<u>74,630</u>	<u>-</u>	<u>-</u>	<u>74,630</u>
Excess (deficit) of revenues over expend	<u>(74,530)</u>	<u>-</u>	<u>77,588</u>	<u>-</u>	<u>77,588</u>
Other Financing Sources (Uses)					
Operating transfers out	-	-	(74,766)	-	(74,766)
Total other financing sources (uses)	<u>-</u>	<u>-</u>	<u>(74,766)</u>	<u>-</u>	<u>(74,766)</u>
Excess (deficit) of revenues and other financing sources over expenditures and other financing uses	<u>(74,530)</u>	<u>-</u>	<u>2,822</u>	<u>-</u>	<u>2,822</u>
Fund balance, beginning	<u>74,530</u>	<u>-</u>	<u>4,750</u>	<u>-</u>	<u>4,750</u>
Fund balance, ending	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 7,572</u>	<u>\$ -</u>	<u>\$ 7,572</u>

The accompanying notes to the required supplementary schedules are an integral part of these financial statements.

Harlan Independent School District
Budgetary Comparison Schedules

Other Supplementary Information
For the year ended June 30, 2008

	Building Fund				Variance
	Budgeted Amounts		Actual	Adjustments	Budget
	Original	Final	GAAP Basis	Budget Basis	Favorable (Unfavorable)
Revenues					
From local sources					
Ad valorem tax	\$ 60,000	\$ 58,500	\$ 58,309	\$ -	\$ (191)
Earnings on investments	-	-	1,757	-	1,757
State sources					
Other	152,471	179,197	186,459	-	7,262
Total revenues	<u>212,471</u>	<u>237,697</u>	<u>246,525</u>	<u>-</u>	<u>8,828</u>
Expenditures					
Facilities acquisition and construction	2,029	128,099	-	-	128,099
Debt Service	114,671	109,598	-	-	109,598
Total expenditures	<u>116,700</u>	<u>237,697</u>	<u>-</u>	<u>-</u>	<u>237,697</u>
Excess (deficit) of revenues over expenditures	<u>95,771</u>	<u>-</u>	<u>246,525</u>	<u>-</u>	<u>246,525</u>
Other Financing Sources (Uses)					
Operating transfers out	(95,771)	-	(107,890)	-	(107,890)
Total other financing sources (uses)	<u>(95,771)</u>	<u>-</u>	<u>(107,890)</u>	<u>-</u>	<u>(107,890)</u>
Excess (deficit) of revenues and other financing sources over expenditures and other financing uses	<u>-</u>	<u>-</u>	<u>138,635</u>	<u>-</u>	<u>138,635</u>
Fund balance, beginning	<u>-</u>	<u>-</u>	<u>2,279</u>	<u>-</u>	<u>2,279</u>
Fund balance, ending	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 140,914</u>	<u>\$ -</u>	<u>\$ 140,914</u>

The accompanying notes to the required supplementary schedules are an integral part of these financial statements.

Harlan Independent School District

**Statement of Revenues, Expenditures and Changes in Fund Balance - Harlan Independent School
Activity Funds**

For the year ended June 30, 2008

	<u>Fund Balance</u> <u>July 1, 2007</u>	<u>Receipts</u>	<u>Disbursement</u>	<u>Transfers In</u>	<u>Transfers Out</u>	<u>Fund Balance</u> <u>June 30, 2008</u>
Harlan Elementary	\$ 8,126	\$ 85,328	\$ 76,345	\$ -	\$ -	\$ 17,109
Harlan High School	94,419	336,900	325,284	-	-	106,035
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
Total	<u>\$ 102,545</u>	<u>\$ 422,228</u>	<u>\$ 401,629</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 123,144</u>

The accompanying notes to the other supplementary schedules are an integral part of these financial statements.

Harlan Independent School District

Statement of Revenues, Expenditures and Changes in Fund Balance - Harlan High School

For the year ended June 30, 2008

	Fund Balance July 1, 2007	Receipts	Disbursement	Fund Balance June 30, 2008
5/6 Boys Basketball	\$ 2,253	\$ 5,625	\$ 4,444	\$ 3,434
5/6 Cheerleaders	779	2,502	3,201	80
5/6 Football	1,076	2,742	3,355	463
5/6 Girls Basketball	2,999	6,310	5,209	4,100
7/8 Boys Basketball	2,047	6,520	5,754	2,813
7/8 Cheerleaders	2,932	9,994	12,630	296
7/8 Football	627	4,381	4,398	610
7/8 Girls Basketball	1,688	4,991	4,990	1,689
Art Fund	24	-	-	24
Athletic CD	10,000	-	-	10,000
Athletic Fund	1,262	3,103	3,311	1,054
Band Fund	1,822	11,731	3,883	9,670
Black Diamond	13,716	24,998	16,014	22,700
Boys Choir	3,063	5,592	5,504	3,151
Boys Tennis	1,844	1,511	1,260	2,095
Business Department	23	-	23	-
Computer Class	263	178	166	275
Dragon Gridiron	150	-	-	150
Dragon Shack	471	1,278	1,632	117
E.R."Doc" Gray Roast	-	3,795	2,903	892
E-Classes	-	2,775	2,775	-
Eighth Grade Account	464	1,233	1,322	375
Extended Studies	66	-	66	-
FBLA	15	-	15	-
FHA	361	-	361	-
Fifth Grade Account	740	1,461	1,633	568
Flower Fund	7	191	183	15
FRYSC / Misc	808	2,127	1,180	1,755
FRYSC / Wellness	1,332	1,291	1,050	1,573
Future Educators	73	-	73	-
Gary Laws Memorial Fund	100	1,000	1,000	100
Gear Up	2,441	361	2,341	461
Girls Basketball - Florida Trip	-	15,801	12,000	3,801
Girls Tennis	2,045	1,319	928	2,436
Golf	936	1,162	1,364	734
H.S. Academic Team	32	-	-	32
H.S. Baseball	-	4,320	4,320	-
H.S. Beta Club	237	806	687	356
H.S. Boys Basketball	6	32,129	32,135	-
H.S. Cheerleaders	1,531	15,548	16,527	552
H.S. Counselor	67	1,639	1,484	222
H.S. Football	1,184	32,275	33,164	295
H.S. Girls Basketball	2,244	33,955	34,924	1,275
Harlan Scholars	-	3,817	3,757	60
HHS Student Bank	-	1,225	1,225	-

The accompanying notes to the other supplementary schedules are an integral part of these financial statements.

Harlan Independent School District

Statement of Revenues, Expenditures and Changes in Fund Balance - Harlan High School

For the year ended June 30, 2008

	Fund Balance July 1, 2007	Receipts	Disbursement	Fund Balance June 30, 2008
Home Economics	163	-	163	-
Instructional Fund	1,831	3,903	5,475	259
Interact Club	271	-	271	-
Junior Class	-	10,814	7,846	2,968
Kevin Hudson Scholarship Fu	-	1,660	500	1,160
Key Club	615	-	615	-
Library Fund	2,861	4,476	4,073	3,264
Little Buddies	303	-	-	303
Locker Fund	37	823	837	23
M.S. Academic Team	20	162	162	20
M.S. Baseball	15	1,369	1,384	-
M.S. Beta Club	486	6,120	4,867	1,739
M.S. Choir	626	2,366	2,854	138
M.S. Football	-	1,826	396	1,430
M.S. Science Club	56	-	-	56
Math Department	334	710	410	634
Musettes	-	2,039	2,039	-
National Honor Society	71	-	71	-
New York Trip	993	-	-	993
PE	225	20	244	1
Pep Club	99	-	99	-
Science Department	596	900	545	951
Senior Class	651	377	789	239
Sixth Grade Account	799	6,036	5,976	859
Softball	1,053	8,337	8,947	443
Spanish	6	-	-	6
Special H	8,827	21,388	26,976	3,239
Special H CD	7,500	-	-	7,500
Student Council	115	-	-	115
Supplemental Books	751	593	1,281	63
The Weekly Dragon	14	-	14	-
Track / Cross Country	258	2,636	2,894	-
Transportation	-	2,760	2,375	385
Volleyball	3,115	7,899	9,990	1,024
Total	<u>\$ 94,419</u>	<u>\$ 336,900</u>	<u>\$ 325,284</u>	<u>\$ 106,035</u>

The accompanying notes to the other supplementary schedules are an integral part of these financial statements.

Schedule of Expenditures of Federal Awards

For the year ended June 30, 2008

Federal Grantor/ Pass Through Grantor/ Program Title	Federal CFDA Number	Pass-Through Grantor's Number	Program or Award Amount	Disbursements	Total per CFDA / Cluster	Total Per Department
U.S. Department of Agriculture:						
<i>Passed through State Department of Education:</i>						
Food Donation	10.550	-	\$ 22,299	\$ 22,299	\$ 22,299	
Total Donation						
School Breakfast Program	10.553	7760005-07	17,764	17,764		
School Breakfast Program	10.553	7760005-08	45,120	45,120		
National School Lunch Program	10.555	7750002-07	54,183	54,183		
National School Lunch Program	10.555	7750002-08	148,126	148,126		
State Match	10.555	7750008-08	4,804	4,804		
Total Child Nutrition Cluster					269,997	
Total U.S. Department of Agriculture						\$ 292,296

U.S. Department of Education						
<i>Passed Through State Department of Education:</i>						
Title I Grant to Local Educational Agencies	84.010	3100002-06	\$ 278,664	\$ 40,375		
Title I Grant to Local Educational Agencies	84.010	3100002-07	264,850	245,991		
Total Title I Grant to Local Educational Agencies					\$ 286,366	
Special Education - Grants to States (IDEA, Part B)	84.027	3810002-06	182,304	116,518		
Special Education - Grants to States (IDEA, Part B)	84.027	3810002-07	183,524	124,580		
Special Education - Preschool Grants (IDEA Preschool)	84.173	3800002-05	17,609	4,126		
Special Education - Preschool Grants (IDEA Preschool)	84.173	3800002-06	17,026	16,878		
Special Education - Preschool Grants (IDEA Preschool)	84.173	3800002-07	15,395	1,268		
Total Special Education Cluster					263,370	
Career and Technical Education - Gasic Brants to States	84.048	3487	6,956	920		
Career and Technical Education - Gasic Brants to States	84.048	3488	6,562	6,562		
Total Career and Technical Education - Gasic Brants to States					7,482	
Safe and Drug-Free Schools and Communities -- State Grants	84.186	3410002-06	5,148	194		
Safe and Drug-Free Schools and Communities -- State Grants	84.186	3410002-07	5,106	4,838		
Total Safe and Drug Free Schools					5,032	
Fund for the Improvement of Education	84.215	5664	983,960	83,562		
Total Fund for the Improvement of Education						83,562

The accompanying notes to the other supplementary schedules are an integral part of these financial statements.

Schedule of Expenditures of Federal Awards

For the year ended June 30, 2008

Federal Grantor/ Pass Through Grantor/ Program Title	Federal CFDA Number	Pass-Through Grantor's Number	Program or Award Amount	Disbursements	Total per CFDA / Cluster	Total Per Department
State Grants for Innovative Programs	84.298	3500002-05	3,062	121		
State Grants for Innovative Programs	84.298	3500002-06	1,337	1,039		
State Grants for Innovative Programs	84.298	3500002-07	1,349	-		
Total State Grants for Innovative Programs					1,160	
Education Technology State Grants	84.318	3210002-05	5,421	2,424		
Education Technology State Grants	84.318	3210002-06	2,793	2,541		
Education Technology State Grants	84.318	3210002-07	2,648	476		
Total Education Technology State Grants					5,441	
Rural Education	84.358	3507	21,294	8,218		
Rural Education	84.358	3508	24,897	13,764		
Total Rural Education					21,982	
Improving Teacher Quality State Grants	84.367	3230002-06	59,212	17,531		
Improving Teacher Quality State Grants	84.367	3230002-07	58,296	54,417		
Total Improving Teacher Quality State Grants					71,948	
Total U.S. Department of Education						746,344
Total Expenditures of Federal Awards						\$ 1,038,640

The accompanying notes to the other supplementary schedules are an integral part of these financial statements.

Harlan Independent School District

Notes to Schedule of Expenditures of Federal Awards

For the Year Ended June 30, 2008

Note A –Basis of Presentation

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the District and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

Note B – Food Distribution

Nonmonetary assistance is reported in the schedule at the fair market value of the commodities received and disbursed. At June 30, 2008, the District had received food commodities totaling \$22,299 in inventory. Since the district no longer tracks commodities individually, all commodities received are considered expended.

Harlan Independent School District

Board Members and Administration Personnel

For the Year Ended June 30, 2008

Board Members

Address

S. Parker Boggs

PO Box 52
Harlan, KY 40831

Rebecca Goss

PO Box 897
Harlan, KY 40831

Terry Harris

PO Box 22
Baxter, KY 40806

Joe Meadors

PO Box 549
Harlan, KY 40831

Kathleen Stacey

203 North Cumberland Avenue
Harlan, KY 40831

Administrative Personnel

David Johnson, Superintendent

Web-site

www.harlan-ind.k12.ky.us

District Address

420 East Central Street
Harlan, Kentucky 40831
(606) 573-8700
(606) 573-8711 fax



Gaw & Associates, PLLC
CERTIFIED PUBLIC ACCOUNTANTS

**Report on Internal Control Over Financial Reporting and on Compliance and Other Matters
Based on An Audit of Financial Statements Performed in Accordance with Government Auditing
Standards**

To the Board of Education
Harlan Independent School District

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Harlan Independent School District, as of and for the year ended June 30, 2008 which collectively comprise the Harlan Independent School District's basic financial statements and have issued our report thereon dated October 31, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; OMB Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations* and the audit requirements prescribed by the Kentucky State Committee for School District Audits in *Guide for Auditing Local School Districts' Fiscal Records*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Harlan Independent School District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Harlan Independent School District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, or prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies described in the accompanying schedule of findings and questioned costs to be significant deficiencies in internal control over financial reporting. (2008-01 thru 2008-05)

A material weakness is a significant deficiency, or combination of significant deficiencies, that result in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that none of the significant deficiencies described above is a material weakness.

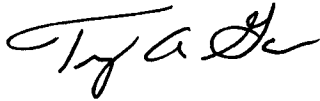
Compliance and Other Matters

As part of obtaining reasonable assurance about whether Harlan Independent School District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* or state audit requirements.

We noted certain matters that we reported to management of Harlan Independent School District in a separate letter dated October 31, 2008

Harlan Independent School District's response to the findings identified in our audit are described in the accompanying schedule of findings and responses. We did not audit Harlan Independent School District's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, members of the Board of Education, others within the entity, the Kentucky Department of Education and the Kentucky State Committee for School District Audits and is not intended to be and should not be used by anyone other than these specified parties.



Troy A. Gaw, CPA
Partner

Gaw, & Associates, PLLC
Harlan, Kentucky

October 31, 2008



Gaw & Associates, PLLC
CERTIFIED PUBLIC ACCOUNTANTS

Report on Compliance with Requirements Applicable to Each Major Program and Internal Control Over Compliance in Accordance with OMB Circular A-133

To the Board of Education
Harlan Independent School District

Compliance

We have audited the compliance of Harlan Independent School District, with the types of compliance requirements described in the U. S. Office of Management and Budget (OMB) Circular A-133 *Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2008. Harlan Independent School District's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Harlan Independent School District's management. Our responsibility is to express an opinion on Harlan Independent School District's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*; and the audit requirements prescribed by the Kentucky State Committee for School District Audits in the *Guide for Auditing Local School Districts' Fiscal Records*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Harlan Independent School District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on Harlan Independent School District's compliance with those requirements.

In our opinion, Harlan Independent School District, complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2008.

Internal Control Over Compliance

The management of Harlan Independent School District is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered Harlan Independent School District's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over compliance.

A *control deficiency* in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect

noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

Harlan Independent School District's response to the finding identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit Harlan Independent School District's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, the Board of Education, others within the entity, the Kentucky Department of Education, the Kentucky State Committee for School District Audits, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.



Troy A. Gaw, CPA
Partner

Gaw, & Associates, PLLC
Harlan, Kentucky

October 31, 2008

Harlan Independent School District
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2008

Section I – Summary of Auditor’s Results

Financial Statements

Type of auditor’s report issued:	Unqualified
Internal control over financial reporting:	
Material weakness identified?	No
Reportable condition identified	
not considered to be material weakness?	No
Noncompliance material to financial statements noted?	No

Federal Awards

Internal Control over major programs:	
Material weakness identified?	No
Reportable condition identified no	
Considered to be material weakness?	No
Type of auditor’s report issued on compliance for major programs:	Unqualified
Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)?	No

Identification of major programs:

Name of Federal Program	CFDA Number(s)
Food Donation	10.550
Food Service Cluster	10.553, 10.555, & 10.559

Dollar threshold used to distinguish between Type A and Type B programs:	\$ 300,000
Auditee qualified as low-risk auditee?	Yes

Harlan Independent School District
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2008

Section II – Financial Statement Findings

Matrix on Conditions:

Location	Condition				
	2008-1	2008-2	2008-3	2008-4	2008-5
Board Office	X	X	X		
High School				X	X
Elementary				X	X
Food Service			X		

2008-01 Fixed Assets

Condition: Fixed assets were not recorded or removed as of the financial statement date.

Criteria: GASB 34 requires that the district maintain a listing of fixed assets owned by the district and that those assets be depreciated over their useful lives.

Cause of Condition: Although a manual schedule of changes was maintained it was not completely entered into the computer to update the schedule until the audit was underway.

Effect of Condition: A misstatement could occur that causes the financial statements to be materially misstated or assets could be misappropriated.

Recommendation: It is recommended that the district maintain its asset listing.

Response: All assets and depreciation will be completed prior to the next audit.

2008-02 District accounting personnel

Condition: The Kentucky Department of Education has not informed the financial staff of the requirement that the district should have the ability to prepare the financial statements and notes to the financial statements in accordance with Generally Accepted Accounting Principles, Government Auditing Standards and standards issued by the American Institute of Certified Public Accountants.

Criteria: Pursuant to GAAP, GASB, and AICPA standards, the District is to have personnel adequately trained to prepare the financial statements and notes to the financial statements in the aforementioned format.

Cause of Condition: Changes in the GAAP, GASB, and AICPA standards as to who is to complete the financial statements.

Effect of Condition: The financial statement could be prepared not in accordance with standards.

Recommendation: It is recommended that the district continue to use the services of a CPA firm to compile the financial statements in the GASB format. Management staff members are highly capable of making all management decisions and are able to perform all management functions. The District has also designated an individual who possess suitable skill and knowledge to oversee the financial statements prepared in GASB format.

Schedule of Findings and Questioned Costs

For the Year Ended June 30, 2008

Response: Although we understand that this is a significant deficiency, the district is continuing to use the services of the auditor to write the financial statements. It is currently legal to do so, however if this should change, we will hire a knowledgeable outside accountant to complete the financial statements.

2008-03 Purchase Order Use

Condition: Purchase orders are not properly being used.

Criteria: The District requires purchase orders to be used on all purchases made with the exception of recurring monthly bills. Purchase orders should be issued before the purchase of the items is obligated.

Cause of Condition: Purchases are being initiated without proper approval.

Effect of Condition: This could cause the District to purchase something that is not in the budget or could cause it to run over budget. It could also cause purchase of items that are not eligible to be paid for by certain funds.

Recommendation: It is recommended that "Red Book" procedures be followed and that all purchases properly use purchase orders.

Response: The district will communicate to all appropriate individuals the need and importance of properly using purchase orders. We will stress the non use of purchase orders will not be tolerated.

2008-04 Purchase Order Use – School Activity Funds

Condition: Purchase orders are not properly being used.

Criteria: The District and "Red Book" requires purchase orders to be used on all purchases made with the exception of recurring monthly bills. Purchase orders should be issued before the purchase of the items is obligated.

Cause of Condition: Purchases are being initiated without proper approval.

Effect of Condition: This could cause the District to purchase something that is not in the budget or could cause it to run over budget. It could cause the School Activity Fund to purchase items that are not in the budget or items that are unallowable to be purchased. It could even cause an individual activity account to have a negative ending balance due to the expenditure not being calculated for before it was incurred.

Recommendation: It is recommended that "Red Book" procedures be followed and that all purchases properly use purchase orders.

Response: We have currently scheduled "Red Book" training and will discuss these issues and solutions during that training.

2008-05 Segregation of duties over bank deposits

Condition: Proper segregation of duties are lacking on the control for bank deposits.

Schedule of Findings and Questioned Costs

For the Year Ended June 30, 2008

- Criteria: "Red Book" requires internal controls exist sufficient to ensure that bank deposits are deposited intact and daily (if over \$100). These controls should included, but are not limited to, (a) each individual check listed on deposit slip, (b) a second party reviewing the deposit slip to ensure that the deposit includes all receipts for the day and signing or initialing the slip, (c) someone other than the person responsible for filling out the deposit ticket, or its review having and having access to the accounting system, taking the deposit to the bank. These controls should also ensure that the deposits are easy to review.
- Cause of Condition: Controls consistent to those described in "Red Book" are not consistently being followed.
- Effect of Condition: Funds could be misappropriated thru the manipulation of deposit tickets and the accounting system thus creating a system where there would not be a way to detect any such activity as a normal course of business.
- Recommendation: It is recommended that "Red Book" procedures be followed and that a proper segregation of duties be instituted.
- Response: We have currently scheduled "Red Book" training and will discuss these issues and solutions during that training.

Section III – Federal Award Findings and Questioned Costs

There were no findings that related to the federal awards.

Harlan Independent School District
Summary Schedule of Prior Audit Findings
For the Year Ended June 30, 2008

No finding noted during previous year.

Harlan Independent School District
Corrective Action Plan
For the Year Ended June 30, 2008

No finding noted for current year.



Gaw & Associates, PLLC
CERTIFIED PUBLIC ACCOUNTANTS

Management Letter

To the Board of Education
Harlan Independent School District

In planning and performing my audit of the financial statements of Harlan Independent School District for the year ended June 30, 2008, I considered the district's internal control structure to determine my auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on the internal control structure.

However, during my audit, I became aware of several matters that are opportunities for strengthening internal controls and operating efficiency. The memorandum that accompanies this letter summarizes my comment and suggestions regarding those matters. A separate report dated October 31, 2008, contains my report on reportable conditions and material weaknesses in the district's internal control structure. This letter does not affect my report dated October 31, 2008, on the financial statements of the Harlan Independent School District.

I will review the status of these comments during my next audit engagement. I have already discussed many of these comments and suggestions with various district personnel, and I will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

Troy A. Gaw, CPA
Partner

Gaw, & Associates, PLLC
Harlan, Kentucky

October 31, 2008

Harlan Independent School District
Schedule of Management Points
For the Year Ended June 30, 2008

Matrix on Conditions:

Condition		
Location	2008-6	2008-7
High School	X	X

2008-06 Invoices

Condition: Invoices were not available for inspection for all expenditures.

Criteria: "Red Book" requires original vendor invoices or in cases where no invoices available, (i.e. referees) a standard invoice be kept.

Cause of Condition: This could be caused by inconsistent filing of invoices, or lack of keeping proper documentation.

Effect of Condition: This could cause improper payment made by the fund.

Recommendation: It is recommended that "Red Book" procedures be followed and that before a payment is approved for payment that all proper documentation be reviewed and that this documentation be kept and properly filed.

Response: We have currently scheduled "Red Book" training and will discuss these issues and solutions during that training.

2008-07 Check signatures

Condition: Checks are being issued with only one signature.

Criteria: "Red Book" requires internal control exist sufficient to ensure that checks are not written and distributed without two signatures to ensure correct payment amounts, vendor, etc.

Cause of Condition: Review of check before issuance did not find that checks only had one signature.

Effect of Condition: Funds could be appropriated without the principal or central fund treasurer's knowledge.

Recommendation: It is recommended that "Red Book" procedures be followed and that all checks issued have two signatures.

Response: We have currently scheduled "Red Book" training and will discuss these issues and solutions during that training.